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No. 9813

United States

Circuit Court of Appeals

For the Ninth Circuit.

Vol 2263

SIGNAL OIL AND GAS COMPANY, a Corporation, Appellant.

vs.

UNITED STATES OF AMERICA, Appellee.

Transcript of Record

Upon Appeals from the District Court of the United States for the Southern District of California, Central Division

PARKER PRINTING COMPANY, 545 SANSOME STREET, SAN FRANCISCO

No. 9813

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[Clerk's Note: When deemed likely to be of an important nature, errors or doubtful matters appearing in the original certified record are printed literally in italic; and, likewise, cancelled matter appearing in the original certified record is printed and cancelled herein accordingly. When possible, an omission from the text is indicated by printing in italic the two words between which the omission seems to occur.]

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NAMES AND ADDRESSES OF ATTORNEYS

For Appellant:

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Los Angeles, California.

For Appellee:

WILLIAM FLEET PALMER, Esq.,
United States Attorney,
E. H. MITCHELL, Esq.,
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ARMOND MONROE JEWELL, Esq.,
Assistant United States Attorney,
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Los Angeles, California. [1*]

*Page numbering appearing at foot of page of original certified Transcript of Record.

In the District Court of the United States in and for the Southern District of California, Central Division.

In Equity No. 1460-Y

UNITED STATES OF AMERICA,
Complainant,

vs.

SIGNAL OIL AND GAS COMPANY,
Defendant.

BILL OF COMPLAINT

To the Honorable Judges of the District Court of the United States for the Southern District of California:

The United States of America, complaining of the above-named defendant, respectfully shows to the Court:

I.

That at all times hereinafter mentioned complainant was and now is a corporation sovereign and body politic.

II.

That the defendant, Signal Oil and Gas Company, is a corporation organized under the laws of the State of Delaware on June 25, 1928, with offices, and doing business, in the city of Los Angeles and within the jurisdiction of this Court.

III.

That this is a suit in equity by the United States of America of a civil nature, arising under the laws

of the United States providing for internal revenue and the collection thereof brought at the direction of the Attorney General, and begun and prosecuted with the sanction, and at the request of, the Commissioner of Internal Revenue, to obtain relief of the defendant, the complainant having no clear, adequate or complete remedy at law, as will more properly appear in succeeding allegations. [2]

IV.

That the Signal Gasoline Company, a corporation now dissolved, was organized under the laws of the State of California on December 15, 1922, and thereafter engaged in the manufacture and sale of gasoline, with offices, and doing business, in the City of Los Angeles, and within the jurisdiction of this Court.

V.

That the Signal Gasoline Corporation, a corporation now dissolved, was organized under the laws of the State of California on February 11, 1924, and thereafter engaged in the manufacture and sale of gasoline, with offices, and doing business, in the City of Los Angeles, and within the jurisdiction of this Court.

VI.

That pursuant to an agreement between the Signal Gasoline Company and the Signal Gasoline Corporation dated May 1, 1924, all the assets and liabilities of the Signal Gasoline Company were

turned over to the Signal Gasoline Corporation, for 400,000 shares of stock of the Signal Gasoline Corporation, and on September 11, 1924, the Signal Gasoline Company was dissolved. The 400,000 shares received by the Signal Gasoline Company in exchange for its assets and liabilities were distributed to its stockholders.

VII.

That the Signal Gasoline Company, Incorporated, a corporation now dissolved, was organized under the laws of the State of California on December 30, 1924, and was as hereinafter indicated a holding company for the stock of the Signal Gasoline Corporation.

VIII.

That on July 31, 1928, the Signal Gasoline Company, Incorporated, owned 419,500 shares of the stock of the Signal Gasoline Corporation, which was 93.22% of the outstanding 450,005 shares of the Signal Gasoline Corporation; the balance of 30,505 shares of the stock outstanding of Signal Gasoline Corporation (4.23%) was owned by individual stockholders of the Signal Gasoline Company, Incorporated. [3]

IX.

That on August 1, 1928, the defendant, Signal Oil and Gas Company, acquired all the assets of the Signal Gasoline Company, Incorporated, which, as noted above, included 93.22% of the stock of

the Signal Gasoline Corporation, in exchange for stock of the Signal Oil and Gas Company.

X.

That on or about November 30, 1928, the defendant, Signal Oil and Gas Company, acquired the remaining 4.23% of the outstanding stock of the Signal Gasoline Corporation from the individual stockholders by exchange for stock of the Signal Oil and Gas Company.

XI.

That the Signal Gasoline Corporation was liquidated as of December 1, 1928, all its assets and liabilities being assigned to its sole stockholder, the defendant Signal Oil and Gas Company, and the Signal Gasoline Corporation was dissolved by court order on December 12, 1928.

XII.

That the income tax return of the now dissolved Signal Gasoline Company for the calendar year 1923 was filed with the Collector of Internal Revenue for the Sixth District of California on March 15, 1924, and its income tax return for the period ended September 11, 1924, was similarly filed on May 13, 1925.

XIII.

That on October 2, 1928, the Commissioner of Internal Revenue addressed a letter to the Signal Gasoline Corporation, as transferee of the Sig-

nal Gasoline Company, notifying it that a deficiency of $468.33 for income taxes for the year 1923 had been determined.

XIV.

That on December 28, 1929, the Commissioner of Internal Revenue addressed a letter to the Signal Gasoline Corporation, as transferee of the Signal Gasoline Company, notifying it that a [4] deficiency of $2,672.53 for income taxes for the period ended September 11, 1924, had been determined.

XV.

That thereafter petitions were filed with the Board of Tax Appeals for a redetermination of the proposed deficiency referred to in Paragraphs XIII and XIV above, and by an order entered on February 16, 1932, the Board of Tax Appeals held that the Signal Gasoline Corporation was liable for the sums indicated as transferee of the Signal Gasoline Company. (Signal Gasoline Corporation vs. Commissioner, 25 B. T. A. 532.)

XVI.

That no further appeal was taken and on September 10, 1932, the Commissioner of Internal Revenue assessed against the Signal Gasoline Corporation for the year 1923 a tax of $468.33, plus interest of $227.96, and for the period ended September 11, 1924, a tax of $2,672.53, plus interest of $1,200.70.

XVII.

That no part of the above taxes with interest so assessed for the year 1923 and for the period ended September 11, 1924, has been paid.

XVIII.

That by reason of the dissolution of the Signal Gasoline Corporation and the distribution of all its assets to the defendant, its sole stockholder, the Signal Gasoline Corporation was and is left without money, assets or property of any kind with which to pay said taxes due the United States.

XIX.

That the net assets which were acquired by the defendant Signal Oil and Gas Company, as sole stockholder of the Signal Gasoline Corporation, as heretofore shown, were in excess of the amount of the above-mentioned taxes with interest for the year 1923 and for the period ended September 11, 1924, and in excess of the amount for which recovery is sought herein. [5]

XX.

That due demand for the payment of said taxes with interest has been made upon the Signal Oil and Gas Company, but said demand has not been complied with and the taxes remain unpaid.

Wherefore, in consideration of the premises and the facts heretofore stated, the complainant comes before the Court and prays:

1. That the Honorable Court order, adjudge and decree that the defendant, Signal Oil and Gas Company, be accountable to complainant and liable for the aforesaid taxes in the sum of $4,569.52, with interest from September 10, 1932, and that said defendant, Signal Oil and Gas Company be ordered to pay to complainant said unpaid taxes with interest.

2. That this Honorable Court order, adjudge and decree that the assets of the Signal Gasoline Corporation which were transferred to the defendant, Signal Oil and Gas Company, constitute a trust fund for the payment of the aforesaid taxes assessed against the Signal Gasoline Corporation, and that the defendant, Signal Oil and Gas Company, shall account to this Court for the aforesaid trust property, and the fund aforesaid be applied to the payment of the said taxes.

3. That the complainant have such other and further relief, general and special, as may appear to the Court to be just and equitable, as well as a decree for costs.

And may it please the Court to grant unto said complainant a writ of subpoena of the United States of America issued out of and under the seal of this Honorable Court, directed to the above-named defendant, and commanding it on a day certain and under certain penalties therein expressed, personally to appear before this Honorable Court, then and there to answer all and singular the premises, and to stand to and perform and abide by such orders, directions and decrees

as may be made against it in the premises, and complainant will ever pray.

BEN HARRISON,
United States Attorney.
E. H. MITCHELL,
Assistant United States Attorney.
ARMOND MONROE JEWELL,
Assistant United States Attorney.
By ARMOND MONROE JEWELL,
Assistant United States Attorney.

[Endorsed]: Filed Sep. 9, 1938. [6]

In the District Court of the United States in and for the Southern District of California, Central Division.

Equity No. 1461-RJ

UNITED STATES OF AMERICA,
Complainant.

vs.

SIGNAL OIL AND GAS COMPANY,
Defendant.

BILL OF COMPLAINT

To the Honorable Judges of the District Court of the United States for the Southern District of California:

The United States of America, complaining of the defendant, respectfully shows to the Court:

I.

That at all times hereinafter mentioned complainant was and now is a corporation sovereign and body politic.

II.

That the defendant, Signal Oil and Gas Company is a corporation organized under the laws of the State of Delaware on June 25, 1928, with offices, and doing business, in the city of Los Angeles, and within the jurisdiction of this Court.

III.

That this is a suit in equity by the United States of America of a civil nature, arising under the laws of the United States providing for internal revenue and the collection thereof, brought at the direction of the Attorney General, and begun and prosecuted with the sanction and at the request of the Commissioner of Internal Revenue, to obtain relief of the defendant, the complainant having no clear, adequate or complete remedy at law, as will more properly appear in succeeding allegations.

[7]

IV.

That the Signal Gasoline Corporation, a corporation now dissolved, was organized under the laws of the State of California on February 11, 1924, and thereafter engaged in the manufacture and sale of gasoline, with offices and doing business in the City of Los Angeles and within the jurisdiction of this court.

V.

That the Signal Gasoline Company, Incorporated, a corporation, now dissolved, was organized under the laws of the State of California on December 30, 1924, and was as hereinafter indicated a holding company for the stock of the Signal Gasoline Corporation.

VI.

That on July 31, 1928, the Signal Gasoline Company, Incorporated, owned 419,500 shares of the stock of the Signal Gasoline Corporation, which was 93.22% of the outstanding 450,005 shares of the Signal Gasoline Corporation; the balance of 30,505 shares of the Signal Gasoline Corporation (4.23%) was owned by individual stockholders.

VII.

That on August 1, 1928, the defendant, Signal Oil and Gas Company, acquired all the assets of the Signal Gasoline Company, Incorporated, which, as noted above, included 93.22% of the stock of the Signal Gasoline Corporation, in exchange for stock of the Signal Oil and Gas Company.

VIII.

That on or about November 30, 1928, the defendant, Signal Oil and Gas Company acquired the remaining 4.23% of the outstanding stock of the Signal Gasoline Corporation from the individual stockholders of the Signal Gasoline Com-

pany, Incorporated, by exchange for stock of the Signal Oil and Gas Company.

IX.

That the Signal Gasoline Corporation was liquidated as of December 1, 1928, all its assets and liabilities being assigned to [8] its sole stockholder, the defendant Signal Oil and Gas Company, and the Signal Gasoline Corporation was dissolved by court order on December 12, 1928.

X.

That the income tax return of the now dissolved Signal Gasoline Corporation for the period from February 11, 1924 (the date of its incorporation) to December 31, 1924 was filed with the Collector of Internal Revenue for the Sixth District of California on May 13, 1925. This period of time is hereinafter referred to as the year 1924.

XI.

That on December 3, 1928, the Signal Gasoline Corporation filed Form 872 extending the period for assessment for any deficiency in tax which might be assessed for the year 1924 until December 31, 1929.

XII.

That on December 28, 1929, the Commissioner of Internal Revenue addressed a letter to the Signal Gasoline Corporation notifying it, in accordance with Section 274 of the Revenue Act of 1926,

that a deficiency of $14,137.05 for income taxes for the year 1924 had been determined. Said notice of deficiency also included a determination with respect to deficiencies in income taxes for the year 1925 and 1926 which are not here involved.

XIII.

That thereafter a petition was filed with the Board of Tax Appeals for a redetermination of the proposed deficiencies referred to in Paragraph XII above, and by an order entered on March 15, 1932, the Board of Tax Appeals determined that the asserted deficiencies were correct. (Signal Gasoline Corporation vs. Commissioner, 25 B. T. A. 861.)

XIV.

That no further appeal was taken with respect to the defi- [9] ciency asserted for the year 1924, and on October 1, 1932, the Commissioner of Internal Revenue assessed against the Signal Gasoline Corporation for the year 1924 a tax of $14,-137.05, plus interest of $6,080.77.

XV.

That no part of the above tax with interest so assessed for the year 1924 has been paid.

XVI.

That by reason of the dissolution of the Signal Gasoline Corporation and the distribution of all its assets to the defendant, its sole stockholder, the Signal Gasoline Corporation was and is left with-

out money, assets or property of any kind with which to pay said tax due the United States.

XVII.

That the net assets which were acquired by the defendant, Signal Oil and Gas Company, as sole stockholder of the Signal Gasoline Corporation, as heretofore shown, were in excess of the above-mentioned tax with interest for the year 1924, and in excess of the amount for which recovery is sought herein.

XVIII.

That due demand for the payment of said tax with interest has been made upon the Signal Oil and Gas Company, but said demand has not been complied with and the tax remains unpaid.

Wherefore, in consideration of the premises and the facts heretofore stated, the complainant comes before the Court and prays:

1. That the Honorable Court order, adjudge and decree that the defendant Signal Oil and Gas Company be accountable to complainant and liable for the aforesaid tax in the sum of $20,217.82 with interest from October 1, 1932, and that said defendant Signal Oil and Gas Company be ordered to pay to complainant said unpaid tax with interest. [10]

2. That this Honorable Court order, adjudge and decree that the assets of the Signal Gasoline Corporation, which were transferred to the defendant, Signal Oil and Gas Company, constitute a

trust fund for the payment of the aforesaid tax assessed against the Signal Gasoline Corporation, and that the defendant, Signal Oil and Gas Company shall account to this Court for the aforesaid trust property, and the fund aforesaid be applied to the payment of the said tax.

3. That the complainant have such other and further relief, general and special, as may appear to the Court to be just and equitable, as well as a decree for cost.

And may it please the Court to grant unto said complainant a writ of subpoena to the United States of America issued out of and under the seal of this Honorable Court, directed to the above-named defendant, and commanding it on a day certain and under certain penalties therein expressed, personally to appear before this Honorable Court, then and there to answer all and singular the premises, and to stand to and perform and abide by such orders, directions and decrees as may be made against it in the premises and complainant will ever pray.

BEN HARRISON,
United States Attorney.
E. H. MITCHELL,
Asst. United States Attorney.
ARMOND MONROE JEWELL,
Asst. United States Attorney.
By ARMOND MONROE JEWELL,
Attorneys for Plaintiff.

[Endorsed]: Filed Sep. 9, 1938. [11]

[Title of District Court and Cause—No. 1460-Y.]

ANSWER

To the Honorable Judges of the District Court of the United States, for the Southern District of California:

The defendant, Signal Oil and Gas Company, answering the bill of complaint on file herein, denies, admits and alleges as follows:

I.

Defendant admits the allegations contained in Paragraph I of the complaint.

II.

Defendant admits the allegations contained in Paragraph II of the complaint.

III.

Defendant has no information or belief as to the matters alleged in Paragraph III of the complaint, and upon such lack of information or belief, denies the allegations contained in Paragraph III of the complaint. [12]

IV.

Defendant admits the allegations contained in Paragraph IV of the complaint.

V.

Defendant admits the allegations contained in Paragraph V of the complaint.

VI.

Defendant denies the allegations contained in Paragraph VI of the complaint.

VII.

Defendant admits that Signal Gasoline Company, Incorporated, a corporation now dissolved, was organized under the laws of the State of California on December 30, 1924. Defendant denies the other allegations contained in Paragraph VII of the complaint.

VIII.

Defendant denies the allegations contained in Paragraph VIII of the complaint.

IX.

Defendant denies the allegations contained in Paragraph IX of the complaint.

X.

Defendant denies the allegations contained in Paragraph X of the complaint.

XI.

Defendant admits that Signal Gasoline Corporation was dissolved by court order on December 12, 1928, and denies the other allegations contained in Paragraph XI of the complaint. [13]

XII.

Defendant admits the allegations contained in Paragraph XII of the complaint.

XIII.

Defendant admits the allegations contained in Paragraph XIII of the complaint.

XIV.

Defendant denies the allegations contained in Paragraph XIV of the complaint, on the ground that Signal Gasoline Corporation was dissolved on December 12, 1928.

XV.

Defendant denies the allegations contained in Paragraph XV of the complaint, on the ground that Signal Gasoline Corporation was dissolved on December 12, 1928.

XVI.

Defendant admits that no further appeal was taken and denies the other allegations contained in Paragraph XVI of the complaint, on the ground that Signal Gasoline Corporation was dissolved on December 12, 1928.

XVII.

Defendant admits the allegations contained in Paragraph XVII of the complaint.

XVIII.

Defendant denies the allegations contained in Paragraph XVIII of the complaint. [14]

XIX.

Defendant denies the allegations contained in Paragraph XIX of the complaint.

XX.

Defendant denies that demand for the payment of said taxes, with interest, has been made on defendant, but admits that the taxes remain unpaid.

For a Second, Separate and Affirmative Defense, Defendant Alleges as Follows:

I.

Defendant alleges that the complaint is barred by the statute of limitations.

II.

The time within which the complainant could sue in equity under the trust fund theory was six (6) years from and after the date the tax had been assessed against the taxpayer, Signal Gasoline Company.

III.

The additional tax demanded in the complaint was never assessed against the taxpayer, Signal Gasoline Company.

IV.

The time for bringing suit against alleged transferees of the assets of Signal Gasoline Company expired on March 15, 1930, and May 13, 1931, with respect to the taxes of Signal Gasoline Company for 1923 and 1924, respectively. [15]

V.

The complaint was filed on September 9, 1938, and is barred by the statute of limitations.

For a Third, Separate and Affirmative Defense, Defendant Alleges as Follows:

I.

That the complaint is barred by the statute of limitations.

II.

That the period within which the complainant could bring suit against an alleged transferee of the assets of Signal Gasoline Company was six (6) years from and after the dates of the assessment of the additional tax against Signal Gasoline Company, or from the dates of the filing of the returns. No assessment of the additional tax was made against Signal Gasoline Company and the returns were filed on March 15, 1924, and May 13, 1925, respectively, for the years 1923 and 1924, and the time for suing alleged transferees expired on March 15, 1930, and May 13, 1931, respectively.

III.

That the purported assessment against Signal Gasoline Corporation for the taxes of Signal Gasoline Company for 1923 and 1924 allegedly made on September 10, 1932, does not start a new six-year period in which to sue an alleged transferee, as the purported assessment made on Signal Gasoline Corporation was absolutely null and void, as that corporation had been dissolved on December 12, 1928, and was not in existence at the date of the alleged assessment. [16]

IV.

The complaint herein was filed on September 9, 1938, and the period for filing the same having expired on March 15, 1930, and May 13, 1931, respectively, for the taxes for the years 1923 and 1924, the complaint herein is barred by the statute of limitations.

Wherefore, defendant prays that complainant take nothing by its complaint, and that defendant be allowed its costs of suit herein.

JOSEPH D. PEELER,
MELVIN D. WILSON,
Attorneys for Defendant, Signal Oil and Gas Company.

[Verified]

[Endorsed]: Filed Sep. 30-1938. [17]

[Title of District Court and Cause—No. 1461-RJ.]

ANSWER

To the Honorable Judges of the District Court of the United States, for the Southern District of California:

That defendant, Signal Oil and Gas Company, answering the bill of complaint on file herein, denies, admits and alleges as follows:

I.

Defendant admits the allegations contained in Paragraph I of the complaint.

II.

Defendant admits the allegations contained in Paragraph II of the complaint.

III.

Defendant has no information or belief as to the matters alleged in Paragraph III of the complaint, and, upon such lack of information or belief, denies the allegations contained in Paragraph III of the complaint. [18]

IV.

Defendant admits the allegations contained in Paragraph IV of the complaint.

V.

Defendant admits that Signal Gasoline Company, Incorporated, a corporation now dissolved, was organized under the laws of the State of California on December 30, 1924, and defendant denies the other allegations contained in Paragraph V of the complaint.

VI.

Defendant denies the allegations contained in Paragraph VI of the complaint.

VII.

Defendant denies the allegations contained in Paragraph VII of the complaint.

VIII.

Defendant denies the allegations contained in paragraph XIII of the complaint.

IX.

Defendant admits that Signal Gasoline Corporation was dissolved by court order on December 12, 1928, and denies all of the other allegations contained in Paragraph IX of the complaint.

X.

Defendant admits the allegations contained in Paragraph X of the complaint. [19]

XI.

Defendant denies the allegation contained in Paragraph XI of the complaint.

XII.

Defendant denies the allegations contained in the first sentence of Paragraph XII of the complaint, on the ground that Signal Gasoline Corporation was dissolved on December 12, 1928.

XIII.

Defendant denies the allegations contained in Paragraph XIII of the complaint on the ground that Signal Gasoline Corporation was dissolved on December 12, 1928.

XIV.

Defendant admits that no further appeal was taken with respect to the deficiency asserted for the year 1924, and denies the other allegations contained in Paragraph XIV of the complaint on the ground that Signal Gasoline Corporation was dissolved on December 12, 1928.

XV.

Defendant admits the allegations contained in Paragraph XV of the complaint.

XVI.

Defendant denies the allegations contained in Paragraph XVI of the complaint.

XVII.

Defendant denies the allegations contained in Paragraph XVII of the complaint. [20]

XVIII.

Defendant denies that demand for the payment of said tax, with interest, has been made upon Signal Oil and Gas Company. Defendant admits that the taxes remain unpaid.

For a Second, Separate and Affirmative Defense, Defendant Alleges as Follows:

I.

Defendant alleges that the complaint is barred by the statute of limitations.

II.

The time within which the complainant could sue in equity under the trust fund theory was six (6) years from and after the date the tax had been assessed against the taxpayer, Signal Gasoline Corporation.

III.

The additional tax demanded in the complaint was never assessed against the taxpayer, Signal Gasoline Corporation, as said corporation was dissolved on December 12, 1928, and the alleged assessment was not purported to have been made until October 1, 1932, and since there was no Signal Gasoline Corporation then in existence, the alleged assessment was void.

IV.

The time for bringing suit against the alleged transferees of the assets of Signal Gasoline Corporation with respect to the taxes of Signal Gasoline Corporation for the year 1924, expired on May 13, 1931, which was six (6) years after the return was filed. [21]

V.

The complaint herein was filed on September 9, 1938, and is barred by the statute of limitations.

Wherefore, defendant prays that the complainant take nothing by its complaint on file herein, and that defendant be allowed its costs of suit herein.

JOSEPH D. PEELER,
MELVIN D. WILSON,
Attorneys for Defendant Signal Oil and Gas Company.

[Verified]

[Endorsed]: Filed Sep. 30-1938. [22]

[Title of District Court and Cause—No. 1461-RJ.]

ORDER TRANSFERRING CASE PURSUANT TO RULE 19

Good cause appearing therefor, It Is Hereby Ordered: That the above-entitled cause be transferred to the Calendar of Judge Yankwich for further proceedings herein.

Los Angeles, California, February 8, 1939.

RALPH E. JENNEY
Judge

LEON R. YANKWICH
Judge

[Endorsed]: Filed Feb. 17, 1939. [23]

[Title of District Court and Cause — No. Eq. 1460-Y.]

STIPULATION.

It Is Hereby Stipulated, by and between the parties hereto, through their respective counsel that this cause may be tried upon the allegations contained in the complaint, and admitted in the answer, and upon the facts stated in this stipulation, and upon such further evidence as either party may introduce at the trial not contradictory thereto.

I.

That this is a suit in equity by the United States of America of a civil nature, arising under the laws

of the United States providing for internal revenue and the collection thereof, brought at the direction of the Attorney General and begun and prosecuted with the sanction and at the request of the Commissioner of Internal Revenue to obtain relief of the defendant; and that the plaintiff has no clear, adequate or complete remedy at law.

II.

That pursuant to an agreement between the Signal Gasoline Company and the Signal Gasoline Corporation dated May 1, 1924, all the assets and liabilities of the Signal Gasoline Company were turned over to the Signal Gasoline Corporation for 400,000 shares of stock of the Signal Gasoline Corporation, and on September 11, 1924, [24] the Signal Gasoline Company was dissolved; the 400,000 shares received by the Signal Gasoline Company in exchange for its assets and liabilities were distributed to its stockholders; that accompanying this stipulation is a true copy of said Agreement which will be offered into evidence and, with leave of Court, marked "Plaintiff's Exhibit A", and filed herewith.

III.

That at all times herein mentioned the Signal Gasoline Company, Inc., a corporation now dissolved, was prior to its dissolution a holding company for the stock of the Signal Gasoline Corporation.

IV.

That on July 31, 1928, the Signal Gasoline Company, Incorporated, owned 419,500 shares of the stock of the Signal Gasoline Corporation, which was 93.22% of the outstanding 450,005 shares of the Signal Gasoline Corporation; the balance of 30,505 shares of the stock outstanding of the Signal Gasoline Corporation (4.23%) was owned by individual stockholders of the Signal Gasoline Company, Incorporated.

V.

That on August 1, 1928, the defendant, Signal Oil and Gas Company, acquired all the assets of the Signal Gasoline Company, Incorporated, which, as noted above, included 93.22% of the stock of the Signal Gasoline Corporation, in exchange for stock of the Signal Oil and Gas Company.

VI.

That on or about November 30, 1928, the defendant, Signal Oil and Gas Company, acquired the remaining 4.23% of the outstanding stock of the Signal Gasoline Corporation [25] from the individual stockholders by exchange for stock of the Signal Oil and Gas Company.

VII.

That the Signal Gasoline Corporation was liquidated as of December 1, 1928, and all its assets and liabilities distributed, as set forth in the stipulation in United States v. Signal Oil & Gas Co., No. Equity 1461-Y.

VIII.

That accompanying this stipulation are true copies of the corporation income tax returns of the Signal Gasoline Company for the calendar year 1923, the amended return of the said company for the same year, the tentative return for the year 1924, and the final return for the year 1924, which will be offered into evidence by plaintiff and with leave of Court marked "Plaintiff's Exhibits B, C. D, and E, respectively, and filed herein.

IX.

That on October 2, 1928, and on December 28, 1929, the Commissioner of Internal Revenue addressed and mailed a letter to the Signal Gasoline Corporation setting forth certain transferee deficiencies; that true and certified photostatic copies of said letters accompany this stipulation which will be offered into evidence by plaintiff and with leave of Court marked "Plaintiff's Exhibits F and G", respectively, and filed herein.

X.

That thereafter petitions in the name of the Signal Gasoline Corporation were filed with the Board of Tax Appeals for a redetermination of the deficiencies so proposed; that said proceedings were docketed under Numbers 41532 and 47620, and on February 16, 1932, the Board of Tax Appeals purported to affirm the ruling of the [26] Commissioner in an opinion reported in 25 B. T. A. 532; that ac-

companying this stipulation are true and certified copies of the petitions and decisions in Board Docket No. 41532, and Board Docket No. 47620 which will be offered into evidence by plaintiff and with leave of Court marked "Plaintiff's Exhibits H and I", respectively, and filed herein.

XI.

That on September 10, 1932, the Commissioner of Internal Revenue purported to assess the Signal Gasoline Corporation as a transferee for the year 1923 a tax of $468.33, plus interest of $227.96; and for the period ended September 11, 1924, a tax of $2,672.53, plus interest of $1200.70; that a true certified photostatic copy of the assessment list accompanies this stipulation and will be offered into evidence by plaintiff and with leave of Court marked "Plaintiff's Exhibit J", and filed herein.

XII.

That by reason of the dissolution of the Signal Gasoline Corporation, and the distribution of its assets as hereinabove stated, the Signal Gasoline Corporation was and is left without money, assets or property of any kind with which to pay the taxes due the United States.

XIII.

That the net assets which were acquired by the defendant Signal Oil and Gas Company, as sole stockholder of the Signal Gasoline Corporation, as heretofore shown, were far in excess of the amount

of the above mentioned taxes with interest for the year 1923, and for the period ended September 11, 1924, and in excess of the amount for which recovery is sought herein. [27]

XIV.

That due demand for the payment of said taxes, with interest, has been made upon the Signal Oil and Gas Company.

XV.

That in the proceedings before the Board of Tax Appeals in Docket Numbers 41532 and 47620, no substitution of parties was ever made, and no motion for such substitution was ever made by either of the parties.

XVI.

That no assessment was ever made against the Signal Oil and Gas Company for the said 1923 and 1924 tax liabilities of the Signal Gasoline Company; that no assessment was ever made against the Signal Gasoline Company for the said 1924 tax liability of the Signal Gasoline Company; but that an assessment against the Signal Gasoline Company was made on July 3, 1931, in the amount of $468.33, plus interest for its said tax liability for the calendar year 1923.

XVII.

That accompanying this stipulation is a true and certified photostat copy of a letter to the Commissioner of Internal Revenue dated January 20, 1932, which will be offered into evidence by the plaintiff

and with leave of Court marked "Plaintiff's Exhibit K", and filed herein.

XVIII.

That at all times herein considered substantially the same persons were Officers and Directors or statutory trustees of the Signal Gasoline Corporation as were the Officers and Directors of Signal Oil and Gas Company and Officers and Directors of the Signal Gasoline Company, Incorporated.

XIX.

That it is the intent of the parties hereto that [28] all of the documents and exhibits herein referred to shall be considered as true copies thereof, that all the signatures thereon are true, that each of the documents shall speak for itself in its legal effect, and that all of the acts of the agents whose names appear on said documents were authorized; save and except, however, that nothing herein shall prevent the defendant from attacking the validity or authority of any of the acts or documents herein referred to, by way of objections to the admissibility of evidence offered at the trial or otherwise, on the grounds that the respective corporate entities were not in existence at the time of the performance of said acts or the execution of said documents, or otherwise.

XX.

That all of the facts, admitted in the pleadings or set forth in the stipulation or found in the ex-

hibits offered, in the case of United States vs. Signal Oil and Gas Company, No. Equity 1461-Y, shall apply herein with the same force and effect and subject to the same objections and reservations, as if pleaded, admitted or proven herein.

Dated: January 16, 1940.

BEN HARRISON,
U. S. Attorney,
E. H. MITCHELL,
Asst. U. S. Attorney
ARMOND MONROE JEWELL,
Asst. U. S. Attorney,
By ARMOND MONROE JEWELL,
Attorneys for Plaintiff.

JOSEPH D. PEELER,
MELVIN D. WILSON,
BY MELVIN D. WILSON,
Attorneys for Defendant.

[Endorsed]: Filed Jan. 16, 1940. [29]

[Title of District Court and Cause — No. Eq. 1461-Y.]

STIPULATION

It Is Hereby Stipulated and Agreed by and between the parties hereto, through their respective counsel, that this cause may be tried upon the allegations contained in the complaint and admitted in the answer, upon the facts stated in this stipulation,

and upon such further evidence as either party may introduce at the trial not contradictory thereto.

I.

That this is a suit in equity by the United States of America of a civil nature arising under the laws of the United States providing for internal revenue and the collection thereof, brought at the direction of the Attorney General and begun and prosecuted with the sanction and at the request of the Commissioner of Internal Revenue to obtain relief of the defendant; and that the plaintiff has no clear, adequate, or complete remedy at law.

II.

That at all times herein mentioned the Signal Gasoline Company, Incorporated, a corporation now dissolved, was prior to its dissolution a holding company for the stock of the Signal Gasoline Corporation.

III.

That on July 31, 1928, the Signal Gasoline Company, [30] Incorporated, owned 419,500 shares of the stock of the Signal Gasoline Corporation, which was 93.22% of the outstanding 450,005 shares of the Signal Gasoline Corporation; the balance of 30,505 shares of the Signal Gasoline Corporation (4.23%) was owned by individual stockholders of the Signal Gasoline Company, Incorporated.

IV.

That on August 1, 1928, the defendant, Signal Oil and Gas Company, acquired all the assets of

the Signal Gasoline Company, Incorporated, which, as noted above, included 93.22% of the stock of the Signal Gasoline Corporation, in exchange for stock of the Signal Oil and Gas Company.

V.

That on or about November 30, 1928, the defendant, Signal Oil and Gas Company, acquired the remaining 4.23% of the outstanding stock of the Signal Gasoline Corporation from the individual stockholders of the Signal Gasoline Company, Incorporated, by exchange for stock of the Signal Oil and Gas Company.

VI.

That the Signal Gasoline Corporation was liquidated as of December 1, 1928, and all of its assets and liabilities were assigned in accordance with a certain instrument of conveyance and the Decree of Dissolution of the Superior Court, true copies of which accompany this stipulation and will be offered into evidence by plaintiff and with leave of the Court marked "Plaintiff's Exhibits 1 and 2", and filed herein.

VII.

That accompanying this stipulation is a true copy of the income tax return of the Signal Gasoline Corporation [31] for the calendar year 1924, which will be offered into evidence and with leave of Court marked "Plaintiff's Exhibit 3", and filed herein.

VIII.

That on December 3, 1928, the Signal Gasoline Corporation signed and filed Form 872, which is entitled "Consent Fixing Period of Limitation upon Assessment of Income and Profits Tax"; that a true and certified photostatic copy of said form accompanies this stipulation, which will be offered into evidence by plaintiff and with leave of Court marked "Plaintiff's Exhibit 4", and filed herein.

IX.

That on December 28, 1929, the Commissioner of Internal Revenue addressed and mailed a letter to the Signal Gasoline Corporation, a true and certified photostatic copy of whi h accompanies this stipulation, and which will be offered into evidence by plaintiff and with leave of Court marked "Plaintiff's Exhibit 5", and filed herein.

X.

That accompanying this stipulation are true and certified photostatic copies of powers of attorney dated November 21, 1928 and November 21, 1929 in the name of Signal Gasoline Corporation; that these will be offered into evidence by plaintiff and with leave of Court marked respectively "Plaintiff's Exhibits 6 and 7", and filed herein.

XI.

That on or about February 24, 1930, a petition was filed with the Board of Tax Appeals for a redetermination of the deficiencies proposed in Plain-

tiff's Exhibit 5 above referred to; that said proceeding was given [32] Docket No. 47621; that a true copy of said petition accompanies this stipulation and will be offered into evidence by plaintiff and with leave of Court marked "Plaintiff's Exhibit 8", and filed herein; that by an order entered on March 15, 1932, the Board of Tax Appeals purported to determine that the asserted deficiencies were correct; and that said opinion of the Board of Tax Appeals is reported in 25 B. T. A. 861.

XII.

That on October 1, 1932, the Commissioner of Internal Revenue purported to assess the Signal Gasoline Corporation for the year 1924, a tax of $14,137.05, plus interest of $6,080.77; that a true and certified photostatic copy of the assessment accompanies this stipulation, which will be offered into evidence by plaintiff and with leave of Court marked "Plaintiff's Exhibit 9", and filed herein.

XIII.

That by reason of the dissolution of the Signal Gasoline Corporation and the distribution of all of its assets as above set forth, the Signal Gasoline Corporation was and is left without money, assets, or property of any kind with which to pay the said tax and interest due to the United States.

XIV.

That the net assets which were acquired by the defendant Signal Oil and Gas Company, as sole

stockholder of the Signal Gasoline Corporation, as heretofore shown, were far in excess of the above mentioned tax with interest for the year 1924, and in excess of the amount for which recovery is sought herein. [33]

XV.

That due demand for the payment of said tax with interest has been made upon the Signal Oil and Gas Company.

XVI.

That accompanying this stipulation are true copies of the following, which will be offered into evidence by plaintiff and, with leave of Court, marked as Plaintiff's Exhibits and filed as follows:

(a) Letter from F. O. Graves to the Commissioner of Internal Revenue, dated December 3, 1928—"Plaintiff's Exhibit 10";

(b) Protest purportedly from the Signal Gasoline Corporation to the Internal Revenue Agent in Charge, dated November 20, 1929—"Plaintiff's Exhibit 11";

(c) Letter to the Commissioner of Internal Revenue in the name of the Signal Gasoline Corporation, Los Angeles, California, dated January 20, 1932—"Plaintiff's Exhibit 12";

(d) Letter to the Commissioner of Internal Revenue in the name of the Signal Gasoline Company, Incorporated, dated January 20, 1932—"Plaintiff's Exhibit 13";

(e) Sixty day letter, dated March 30, 1931, to the Signal Gasoline Corporation from the Commis-

sioner of Internal Revenue with certain applicable portions of the statement therein attached—"Plaintiff's Exhibit 14";

(f) Applicable portions of revenue agent's report, dated as of August 26, 1930—"Plaintiff's Exhibit 15";

(g) Letter to Collector of Internal Revenue at Los Angeles, dated July 27, 1931, signed by J. H. Rounsavell—"Plaintiff's Exhibit 16";

(h) Offers in compromise in the name of Signal Gasoline Corporation under the respective dates of October [34] 21, 1932, and January 23, 1933—"Plaintiff's Exhibits 17 and 18";

(i) Income tax return of the Signal Gasoline Company, Incorporated, and Subsidiaries for the period of January 1 to July 31, 1928—"Plaintiff's Exhibit 19";

(j) Corporation income tax return of the Signal Oil and Gas Company, and Subsidiaries for the period ended December 31, 1928—"Plaintiff's Exhibit 20"; and

(k) Petition accompanying application of the Signal Oil and Gas Company to issue stock, filed July 23, 1928, and application filed October 6, 1928 —"Plaintiff's Exhibit 21".

XVII.

That in the proceedings before the Board of Tax Appeals in Docket Number 47621, no substitution of parties was ever made, and no motion for such substitution was ever made by either of the parties.

XVIII.

That at all times herein considered substantially the same persons were Officers and Directors or statutory trustees of the Signal Gasoline Corporation as were the Officers and Directors of Signal Oil and Gas Company and Officers and Directors of Signal Gasoline Company, Incorporated.

XIX.

That it is the intent of the parties hereto that all of the documents and exhibits herein referred to shall be considered as true copies thereof, that all the signatures thereon are true, that each of the documents shall speak for itself in its legal effect, and that all of the acts of the agents whose names appear on said documents were authorized; save and except, however, that nothing herein shall prevent the defendant from attacking [35] the validity or authority of any of the acts or documents herein referred to, by way of objections to the admissibility of evidence offered at the trial or otherwise, on the grounds that the respective corporate entities were not in existence at the time of the performance of said acts or the execution of said documents, or otherwise.

XX.

That all of the facts, admitted in the pleadings or set forth in the stipulation, or found in the exhibits offered, in the case of United States vs. Signal Oil and Gas Company, No. Equity 1460-Y, shall apply herein with the same force and effect and

subject to the same objections and reservations, as if pleaded, admitted or proven herein.

Dated: January 16, 1940.

BEN HARRISON,
U. S. Attorney,
E. H. MITCHELL,
Asst. U. S. Attorney,
ARMOND MONROE JEWELL,
Asst. U. S. Attorney,
By ARMOND MONROE JEWELL
Attorneys for Plaintiff.

JOSEPH D. PEELER
MELVIN D. WILSON
By MELVIN D. WILSON
Attorneys for Defendant.

[Endorsed]: Filed Jan. 16, 1940. [36]

At a stated term, to wit: The September Term, A. D. 1939 of the District Court of the United States of America, within and for the Central Division of the Southern District of California, held at the Court Room thereof, in the City of Los Angeles on Tuesday the 16th day of January in the year of our Lord one thousand nine hundred and forty.

Present:

The Honorable: Leon R. Yankwich, District Judge.

[Title of Cause—No. 1460-Y Equity.]

[Title of Cause—No. 1461-Y Equity.]

These causes coming on for trial; A. M. Jewell, Assistant U. S. Attorney, appearing as counsel for the Government; Melvin D. Wilson, Esq., appearing as counsel for the defendant; and Arthur Edwards, court reporter, being present:

It is ordered that these causes be consolidated.

Attorney Wilson makes opening statement in behalf of the defendant.

Pursuant to stipulation, amended and supplemental answer in Case No. 1461 is ordered filed, and stipulation of facts is ordered filed in each case.

* * * * * * *

Stipulation is entered into by counsel re assessments. Both sides rest.

It is ordered that these consolidated causes be submitted on briefs to be filed 30 x 60 x 15. [37]

[Title of District Court and Cause.—No. 1461-RJ.]

AMENDED AND SUPPLEMENTAL ANSWER

To the Honorable Judges of the District Court of the United States, for the Southern District of California:

The defendant, Signal Oil and Gas Company, having obtained permission of the Court therefor,

makes this amended and supplemental answer to the bill of complaint on file herein and, in so doing, denies, admits and alleges as follows:

I.

Defendant adopts, repeats and incorporates herein by reference Paragraphs I to XVIII of its original answer on file herein, as its first defense.

II.

Defendant adopts, repeats and incorporates herein by reference Paragraphs I to V of its second, separate and affirmative defense set out in its original answer on file herein, as its second defense in this amended and supplemental answer.

[38]

For a Third, Separate and Affirmative Defense, Defendant Alleges as Follows:

I.

Defendant alleges that the bill of complaint is barred by the statute of limitations.

II.

That the time for bringing suit against the alleged transferees of the assets of Signal Gasoline Corporation with respect to taxes of Signal Gasoline Corporation for the year 1924, was six years from the time the return was filed, namely six years from May 13, 1925, or six years from the time the tax was validly assessed against the taxpayer, Signal Gasoline Corporation.

III.

Signal Gasoline Corporation, having been dissolved in December of 1928, and the purported assessment not having been made until October 1, 1932, it was invalid and null and void as to Signal Gasoline Corporation.

IV.

If the assessment made on October 1, 1932, was valid, it must of necessity have been made against the trustee of the dissolved Signal Gasoline Corporation, who, upon dissolution, received its assets for the purpose of paying its debts and collecting its accounts. Such trustees constitute the first transferees of the assets of Signal Gasoline Corporation, but a valid assessment against them would not give the plaintiff six years within which to sue subsequent transferees of the assets of Signal Gasoline Corporation. [39]

V.

The suit herein, not having been brought by May 13, 1931, was barred by the statute of limitations.

Wherefore, defendant prays that plaintiff take nothing by its complaint on file herein, and that the defendant be allowed its costs of suit herein.

JOSEPH D. PEELER,
MELVIN D. WILSON,
Attorneys for Defendant Signal Oil and Gas Company.

(Verified)

[Endorsed]: Filed Jan. 16, 1940. [40]

[Title of District Court and Cause.—No. 1460-Y.]

MINUTE ORDER

This cause having been heard upon the issues raised by the Complaint and the Answer, and a stipulation of facts and evidence, oral and documentary, having been introduced, and the cause having been submitted to the Court for decision, and the Court having considered the evidence and the law and the arguments and briefs of counsel, now finds in favor of the plaintiffs and orders that the plaintiff do have and recover of the defendant in the sum of $4,569.52, with interest thereon from September 10, 1932.

As a guide to counsel in the preparation of findings, the Court states the following conclusions upon the issues raised in this and the companion case this day decided also. (1461-Y)

The Court is of the view that under the authority of McPherson vs. Commissioner of Internal Revenue, 9 Cir., 1932, 54 F(2) 751, the deficiency assessment was in all respects valid. The deficiency assessment against the Signal Gasoline Corporation was not an assessment against its directors as transferees of the assets. It was an assessment against it for tax liability incurred during its corporate existence. This being the case, the defendants are not in a position to invoke the doctrine of United States vs. Continental National Bank and Trust [41] Company, 1939, 305 U. S. 398. In other words, the Court is of the view that we are not dealing

here with the transferee of a transferee and that the actions in this and the companion case were timely and are not barred by the Statute of Limitations.

Findings and judgment to be prepared by counsel for the plaintiff under Local Rule 8.

Dated this 27th day of July, 1940.

Counsel notified. [42]

[Title of District Court and Cause.—No. 1461-Y.]

MINUTE ORDER

This cause having been heard upon the issues raised by the Complaint and the Answer, and a stipulation of facts and evidence, oral and documentary, having been introduced, and the cause having been submitted to the Court for decision, and the Court having considered the evidence and the law and the arguments and briefs of counsel, now finds in favor of the plaintiffs and orders that the plaintiff do have and recover of the defendant in the sum of $20,217.82, with interest thereon from September 10, 1932.

As a guide to counsel in the preparation of findings, the Court states the following conclusions upon the issues raised in this and the companion case this day decided also. (1460-Y)

The Court is of the view that under the authority of McPherson vs. Commissioner of Internal Revenue, 9 Cir., 1932, 54 F(2) 751, the deficiency

assessment was in all respects valid. The deficiency assessment against the Signal Gasoline Corporation was not an assessment against its directors as transferees of the assets. It was an assessment against it for tax liability incurred during its corporate existence. This being the case, the defendants are not in a position to invoke the doctrine of United States vs. Continental National Bank and Trust Company, 1939, 305 U. S. 398. In other [43] words, the Court is of the view that we are not dealing here with the transferee of a transferee and that the actions in this and the companion case were timely and are not barred by the Statute of Limitations.

Findings and judgment to be prepared by counsel for the plaintiff under Local Rule 8.

Dated this 27th day of July, 1940.

Counsel notified. [44]

In the District Court of the United States in and for the Southern District of California, Central Division.

No. Eq. 1460-Y

UNITED STATES OF AMERICA,

Plaintiff.

vs.

SIGNAL OIL AND GAS COMPANY,

Defendant.

No. Eq. 1461-Y

UNITED STATES OF AMERICA,

Plaintiff,

vs.

SIGNAL OIL AND GAS COMPANY,

Defendant.

FINDINGS OF FACT AND CONCLUSIONS OF LAW

The above entitled cases having come on for trial on the 16th day of January, 1940, before the Honorable Leon R. Yankwich, United States District Judge, sitting without a jury, plaintiff being represented by the United States Attorney, and Edward H. Mitchell, Assistant United States Attorney, by Armond Monroe Jewell, Assistant United States Attorney, and defendant being represented by Joseph D. Peeler, Esq., and Melvin D. Wilson, Esq., by Melvin D. Wilson, Esq., and a stipulation

of facts having been filed and the court having ordered the consolidation of the above entitled cases for the purpose of trial, and documentary evidence having been offered on behalf of the plaintiff, the court now makes its Findings of Fact and Conclusions of Law:

FINDINGS OF FACT

I.

That these are suits in equity by the United States of America of a civil nature arising under the laws of the United States providing for internal revenue and the collection thereof, brought on [45] September 9, 1938, at the direction of the Attorney General and begun and prosecuted with the sanction and at the request of the Commissioner of Internal Revenue to obtain relief of the defendant; and that the plaintiff has no clear, adequate, or complete remedy at law.

II.

That pursuant to and in accordance with an agreement between the Signal Gasoline Company, a California corporation, and the Signal Gasoline Corporation, a California corporation, dated May 1, 1924, all the assets of the Signal Gasoline Company were turned over to the Signal Gasoline Corporation for 400,000 shares of stock of the Signal Gasoline Corporation, and on September 11, 1924, the Signal Gasoline Company was dissolved; the 400,000 shares received by the Signal Gasoline

Company in exchange for its assets and liabilities were distributed to its stockholders; that "Plaintiff's Exhibit A" is a true copy of the said agreement.

III.

That at all times herein mentioned the Signal Gasoline Company, Incorporated, a corporation now dissolved, was prior to its dissolution a holding company for the stock of the Signal Gasoline Corporation.

IV.

That on July 31, 1928, the Signal Gasoline Company, Incorporated, owned 419,500 shares of the stock of the Signal Gasoline Corporation, which was 93.22% of the outstanding 450,005 shares of the Signal Gasoline Corporation; the balance of 30,505 shares of the stock outstanding of the Signal Gasoline Corporation (4.23%) was owned by individual stockholders of the Signal Gasoline Company, Incorporated.

V.

That on August 1, 1928, the defendant, Signal Oil and Gas Company, acquired all the assets of the Signal Gasoline Company, Incorporated, which, as noted above, included 93.22% of the stock of the Signal Gasoline Corporation, in exchange for stock of the Signal [46] Oil and Gas Company.

VI.

That on or about November 30, 1928, the defendant, Signal Oil and Gas Company, acquired

the remaining 4.23% of the outstanding stock of the Signal Gasoline Corporation from the individual stockholders of the Signal Gasoline Company, Incorporated, by exchange for stock of the Signal Oil and Gas Company.

VII.

That the Signal Gasoline Corporation was liquidated as of December 1, 1928, and all of its assets and liabilities were assigned in accordance with a certain instrument of conveyance and the Decree of Dissolution of the Superior Court; that plaintiff's Exhibits 1 and 2, respectively, are true copies of the said instrument of conveyance and the Decree of Dissolution.

VIII.

That plaintiff's Exhibit B is a true copy of the corporation income tax return of the Signal Gasoline Company for the calendar year 1923; that plaintiff's Exhibit C is a true copy of the amended corporation income tax return of the Signal Gasoline Company for the calendar year 1923; that plaintiff's Exhibit D is a true copy of the tentative corporation income tax return of the Signal Gasoline Company for the year 1924; that plaintiff's Exhibit E is a true copy of the final corporation income tax return of the Signal Gasoline Company for the calendar year 1924, all of which returns were duly filed by or on behalf of the Signal Gasoline Company, on March 15, 1924, May 13, 1925, March 16, 1925 and May 13, 1925, respectively.

IX.

That on October 2, 1928, and again on December 28, 1929, the Commissioner of Internal Revenue duly addressed and mailed a letter to the Signal Gasoline Corporation setting forth certain transferee deficiencies; that said letters, and each of them were duly received by or on behalf of the Signal Gasoline Corporation; that plaintiff's [47] Exhibit F is a true copy of the letter dated October 2, 1928; that plaintiff's Exhibit G is a true copy of the letter dated December 28, 1929.

X.

That thereafter petitions in the name of the Signal Gasoline Corporation were filed by the Signal Gasoline Corporation with the Board of Tax Appeals for a redetermination of the deficiencies proposed in the said letters dated October 2, 1928, and December 28, 1929; that the appeal from the deficiencies proposed in the letter of October 2, 1928, was, on November 19, 1928, docketed with the Board of Tax Appeals under Number 41532; that the appeal from the deficiencies proposed in the letter of December 28, 1929, was on February 24, 1930 docketed with the Board of Tax Appeals under Number 47620; that the petition was signed by six persons and stated that they were the statutory trustees of Signal Gasoline Corporation, a dissolved corporation, acting through its statutory trustees; that on February 16, 1932, the Board of Tax Appeals duly affirmed the ruling of the Commissioner of Internal Revenue in asserting the

deficiencies therein appealed from; that said decision of the Board of Tax Appeals is contained in an opinion reported in 25 Board of Tax Appeals 532; that plaintiff's Exhibit H is a true and certified copy of the petition and decision in the said Board of Tax Appeals docket No. 41532; that plaintiff's Exhibit I is a true and certified copy of the petition and decision in Board of Tax Appeals docket No. 47620.

XI.

That on September 10, 1932, the Commissioner of Internal Revenue duly assessed the Signal Gasoline Corporation, as a transferee of the Signal Gasoline Company, for the above described tax liabilities of the Signal Gasoline Company in the amounts and for the taxable periods as follows:

[48]

For the taxable year 1923—$468.33, plus interest of $227.96.

For the taxable period ended, September 11, 1924—$2,672.53, plus interest of $1,200.70.

That plaintiff's Exhibit J is a true and certified photostatic copy of the assessment lists of the Commissioner of Internal Revenue setting forth the assessments herein described.

XII.

That plaintiff's Exhibit 3 is a true copy of the income tax return filed on May 13, 1925 by the Signal Gasoline Corporation for the calendar year 1924.

XIII.

That on December 3, 1928, the Signal Gasoline Corporation signed and filed Form 872, which is entitled "Consent Fixing Period of Limitation upon Assessment of Income and Profits Tax", thereby extending the statute of limitations for the assessment of deficiencies on account of the Signal Gasoline Corporation's tax liability for the calendar year 1924; that plaintiffs' Exhibit 4 is a true copy of the said form.

XIV.

That on December 28, 1929 the Commissioner of Internal Revenue duly addressed and mailed a letter to the Signal Gasoline Corporation; that this letter proposed an assessment of additional tax liabilities against the Signal Gasoline Corporation on account of a deficiency for the calendar year 1924; that the said letter also proposed an assessment of other additional tax liabilities for the calendar years 1925 and 1926; that plaintiff's Exhibit 5 is a true copy of the said letter.

XV.

That under date of November 21, 1928 the Signal Gasoline Corporation executed a power of attorney to certain attorneys authorizing the said attorneys to represent the Signal Gasoline Corporation before [49] the Treasury Department of the United States and the United States Board of Tax Appeals with reference to the tax liabilities of the

Signal Gasoline Corporation for the calendar years 1924 and 1925; that said power of attorney was signed by S. B. Mosher and O. W. March, President and Secretary respectively of the Signal Gasoline Corporation; that plaintiff's Exhibit 6 is a true copy of the said power of attorney.

XVI.

That under date of November 20, 1929 a power of attorney was executed whereby certain attorneys were authorized to represent the Signal Gasoline Corporation before the Treasury Department and the Board of Tax Appeals in connection with the tax liabilities of the said corporation for the calendar years 1926 and 1927. The said power of attorney was executed in the name of the Signal Gasoline Corporation, but stated that it was a dissolved corporation acting through its statutory trustees, and was signed on the margin thereof by each of the statutory trustees of the dissolved Signal Gasoline Corporation; that plaintiff's Exhibit 7 is a true copy of the said power of attorney.

XVII.

That on or about February 24, 1930 a petition was filed with the Board of Tax Appeals for a redetermination of the deficiencies proposed in plaintiff's Exhibit 5 above referred to; that said proceeding was therein given docket No. 47621; that said petition was filed under the name of the Signal Gasoline Corporation. However, in the body of the petition there was an allegation stating that

"the petitioner is a dissolved California corporation acting through its statutory trustees * * *". The petition was verified by all of the statutory trustees; that plaintiff's Exhibit 8 is a true copy of the said petition to the Board of Tax Appeals; that by an order entered on March 15, 1932 the Board of Tax Appeals determined that the deficiencies asserted therein by the Commissioner of Internal Revenue were correct; that the opinion of the Board of Tax Appeals regarding this matter is reported in 25 Board of Tax Appeals 861. [50]

XVIII.

That on October 1, 1932, pursuant to the said adjudication by the Board of Tax Appeals, referred to in the preceding paragraph, the Commissioner of Internal Revenue duly assessed the Signal Gasoline Corporation for its tax deficiency for the calendar year 1924 in the principal amount of $14,137.05, plus interest of $6,080.77; that plaintiff's Exhibit 9 is a true copy of the assessment list of the Commissioner, upon which there appears the said assessment against the Signal Gasoline Corporation.

XIX.

That by reason of the dissolution of the Signal Gasoline Corporation and the disbursement of all of its assets to its statutory trustees, as above set forth, the Signal Gasoline Corporation was and is left without any money, assets or property of any kind with which to pay the said taxes and interest due to the United States.

XX.

That the assets which were acquired by the defendant Signal Oil and Gas Company, as sole stockholder of the Signal Gasoline Corporation, as heretofore shown, were far in excess of the taxes and interest prayed for in the Complaints herein.

XXI.

That due demand for the payment of the taxes and interest prayed for in the Complaints herein has been made upon the Signal Oil and Gas Company, but no portion thereof has been paid.

XXII.

That at all times herein mentioned and considered substantially the same persons were officers and directors or statutory trustees of the Signal Gasoline Corporation as were the officers and directors of the Signal Oil and Gas Company and officers and directors of the Signal Gasoline Company, Incorporated. [51]

XXIII.

That in the proceedings before the Board of Tax Appeals under docket numbers 41532, 47620 and 47621, no substitution of parties was ever made and no motion for such substitution was ever made by either of the parties.

XXIV.

That all of the Exhibits filed by plaintiff herein are true copies of the originals thereof.

XXV.

That in addition to the acts heretofore described, the statutory trustees of the Signal Gasoline Corporation after its dissolution, who were those persons who were the officers and directors of the defendant, persisted in transacting business affairs of the dissolved corporation in the name of the Signal Gasoline Corporation and in particular in the negotiations with the United States of America regarding the tax liabilities of the Signal Gasoline Corporation.

XXVI.

That no assessment was ever made against the Signal Oil and Gas Company for the 1923 and 1924 tax liabilities of the Signal Gasoline Company; that no assessment was ever made against the Signal Oil and Gas Company for the tax liabilities due from the Signal Gasoline Corporation for the year 1924; that no assessment was ever made against the Signal Gasoline Company for the said 1924 tax liability of the Signal Gasoline Company; that an assessment against the Signal Gasoline Company was made on July 3, 1931, in the amount of $468.33 plus interest for its said tax liability for the calendar year 1923.

XXVII.

On May 13, 1929, a corporation income tax return was filed with the Collector of Internal Revenue at Los Angeles, California on behalf of the Signal Gasoline Corporation and was signed by

S. B. Mosher, as President, and O. W. Marsh, as Treasurer of the said corporation. In said return it was stated in Affiliation Schedule No. 3 thereof that [52] the Signal Gasoline Corporation had been dissolved in December of 1928; that plaintiff's Exhibit 20 is a true copy of the said return.

XXVIII.

In the Revenue Agent's report, dated August 26, 1930, it was stated that the Signal Gasoline Corporation had distributed all of its assets to its stockholders upon its dissolution in December 1928; that plaintiff's Exhibit 15 is a true copy of those portions of the said Revenue Agent's report, which contain those statements. In the letter, dated March 30, 1931 from the Commissioner of Internal Revenue and addressed to the Signal Gasoline Corporation, which letter was the 60 day letter proposing additional taxes for the year 1928, it was stated that the Signal Gasoline Corporation had been dissolved in December 1928; that plaintiff's Exhibit 14 is a true copy of said letter.

CONCLUSIONS OF LAW

I.

That the assessments by the Commissioner of Internal Revenue against the Signal Gasoline Corporation, described in Paragraphs XI and XVIII of the Findings of Fact herein, are correct, timely and valid.

II.

That the said proceedings before the Board of Tax Appeals, the said decisions of the Board of Tax Appeals and the said assessments by the Commissioner of Internal Revenue are valid.

III.

That the actions herein are not barred by the statute of limitations and, therefore, have been timely commenced.

IV.

That the defendant is estopped from setting up the bar of the statute of limitations to the causes of action set forth in Complaints No. 1460-Y and No. 1461-Y. [53]

V.

That the transfer of the assets of the Signal Gasoline Corporation to the defendant as its sole stockholder impressed those assets with a trust for the benefit of the creditors of the Signal Gasoline Corporation and for the benefit of the United States of America in the assertion of its claim for unpaid taxes due from the Signal Gasoline Corporation.

VI.

That plaintiff is entitled to judgment against the defendant in the sum of $20,217.82, together with interest as provided by law from October 1, 1932 and in the sum of $4,569.52, together with interest as provided by law from September 10, 1932.

Dated: This 26th day of December, 1940.

LEON R. YANKWICH,
United States District Judge.

Approved as to form as provided by Rule 8:
JOSEPH D. PEELER and
MELVIN D. WILSON.
By MELVIN D. WILSON,
Attorneys for Defendant.

[Endorsed]: Filed Dec. 26, 1940. [54]

In the District Court of the United States in and for the Southern District of California, Central Division.

No. Eq. 1460-Y

UNITED STATES OF AMERICA,
Plaintiff,

vs.

SIGNAL OIL AND GAS COMPANY,
Defendant.

No. Eq. 1461-Y

UNITED STATES OF AMERICA,
Plaintiff,

vs.

SIGNAL OIL AND GAS COMPANY,
Defendant.

JUDGMENT

The above entitled cases having come on for trial on the 16th day of January, 1940, before the

Honorable Leon R. Yankwich, United States District Judge, sitting without a jury, plaintiff being represented by the United States Attorney, and Edward H. Mitchell, Assistant United States Attorney, by Armond Monroe Jewell, Assistant United States Attorney, and defendant being represented by Joseph D. Peeler, Esq., and Melvin D. Wilson, Esq., by Melvin D. Wilson, Esq., and a stipulation of facts having been filed and the court having ordered the consolidation of the above entitled causes for the purpose of trial, and documentary evidence having been offered on behalf of the plaintiff; and the Court having made its Findings of Fact and Conclusions of Law;

Now, therefore, it is ordered, adjudged and decreed that plaintiff have judgment against the defendant in the sum of twenty thousand two hundred [55] and seventeen dollars eighty-two cents ($20,217.82) together with interest at the rate of 12% per annum from October 1, 1932 to October 24, 1933, and interest at the rate of 6% per annum from October 24, 1933 to the date of payment; and in the sum of four-thousand five hundred and sixty-nine dollars fifty-two cents ($4,569.52) together with interest at the rate of 12% per annum from September 10, 1932 to October 24, 1933, and interest at the rate of 6% per annum from October 24, 1933 to date of payment, to-

gether with costs in the sum of ($27.14) ($27.06) dollars.

Dated: This 26th day of December, 1940.

LEON R. YANKWICH,
United States District Judge.

Approved as to form as provided by Rule 8:
JOSEPH D. PEELER and
MELVIN D. WILSON.
By MELVIN D. WILSON,
Attorneys for Defendant.

Judgment entered Dec. 26, 1940.
Docketed Dec. 26, 1940.
C. O. Book 4, Page (170) (172).

R. S. ZIMMERMAN,
Clerk.
By LOUIS J. SOMERS,
Deputy.

[Endorsed]: Filed Dec. 26, 1940. [56]

[Title of District Court and Cause—No. Eq. 1460-Y]

NOTICE OF APPEAL

Notice is hereby given that Signal Oil and Gas Company, a corporation, defendant above named, hereby appeals to the United States Circuit Court of Appeals for the Ninth Circuit from that certain judgment entered in the above entitled action

on the 26th day of December, 1940, in which action United States of America is plaintiff.

The judgment in the above case and in United States of America vs. Signal Oil and Gas Company, No. Eq. 1461-Y, was entered as a consolidated judgment.

Dated: March 17, 1941.

MELVIN D. WILSON,
JOSEPH D. PEELER,
Attorneys for Defendant.

Copies mailed to U. S. Atty. 3-20-41.

R. S. ZIMMERMAN,
Clerk.
By E. L. S.

[Endorsed]: Filed Mar. 20, 1941. [57]

[Title of District Court and Cause—No. Eq. 1461-Y.]

NOTICE OF APPEAL

Notice is hereby given that Signal Oil and Gas Company, a corporation, defendant above named, hereby appeals to the United States Circuit Court of Appeals for the Ninth Circuit from that certain judgment entered in the above entitled action on the 26th day of December, 1940, in which United States of America is plaintiff.

The judgment in the above case and in United States of America vs. Signal Oil and Gas Com-

pany, No. Eq. 1460-Y, was entered as a consolidated judgment.

Dated: March 17, 1941.

MELVIN D. WILSON,
JOSEPH D. PEELER,
Attorneys for Defendant.

Copies mailed to U. S. Atty. 3-20-41.

R. S. ZIMMERMAN,
Clerk.
By E. L. S.

[Endorsed]: Filed Mar. 20, 1941. [58]

[Title of District Court and Cause—Nos. 1460-Y and 1461-Y.]

STIPULATION FOR CONSOLIDATED RECORD ON APPEAL

It is hereby stipulated by and between the respective parties hereto, through their respective counsel, that the above entitled causes of action, having been consolidated for the purpose of trial, may be consolidated for the purpose of appeal and that one record on appeal will be sufficient and satisfactory for the purpose of appealing both cases.

Dated: March 19, 1941.

WM. FLEET PALMER
United States Attorney
E. H. MITCHELL
Asst. United States Attorney
ARMOND MONROE JEWELL
Asst. United States Attorney
By ARMOND MONROE JEWELL
Attorneys for Plaintiff.
MELVIN D. WILSON
JOSEPH D. PEELER
Attorneys for Defendant. [59]

It is so ordered this 20th day of March, 1941, at 4:40 P. M.

PAUL J. McCORMICK
United States District Judge.

[Endorsed]: Filed Mar. 20, 1941. [60]

[Title of District Court and Cause—Nos. 1460-Y and 1461-Y.]

STIPULATION FOR ORDER EXTENDING TIME FOR FILING RECORD ON APPEAL AND DOCKETING THE ACTION AND ORDER.

It is hereby stipulated by and between the respective parties hereto, through their respective counsel, that the Court may extend the time for filing the record on appeal and docketing the action

in the above entitled causes, from April 26, 1941 to May 11, 1941.

Dated: April 24, 1941.

WM. FLEET PALMER
United States Attorney
E. H. MITCHELL
Asst. United States Attorney
ARMOND MONROE JEWELL
Asst. United States Attorney
By ARMOND MONROE JEWELL
Attorneys for Plaintiff.
MELVIN D. WILSON
JOSEPH D. PEELER [61]

ORDER

Upon filing the foregoing Stipulation of the parties,

It Is Ordered that the appellant may have from April 26, 1941 to May 11, 1941 within which to file the record on appeal and docket the action in the above entitled cases.

Apr. 24, '41, at 3:45 P. M.

PAUL J. McCORMICK
Judge.

[Endorsed]: Filed Apr. 24, 1941. [62]

[Title of District Court and Cause—Nos 1460-Y and 1461-Y.]

STIPULATION DESIGNATING RECORD ON APPEAL

Pursuant to Rule 75 (f) of The Federal Rules of Civil Procedure, it is hereby stipulated by and between the parties hereto, through their respective counsel, that the following shall constitute the Record on Appeal in the above entitled cases:

1. Order Transferring Case, Pursuant to Rule 19, dated February 8, 1939 (Case No. 1461 R. J.)
2. Complaint (Case No. 1460-Y)
3. Complaint (Case No. 1461-Y)
4. Answer (Case No. 1460-Y)
5. Answer (Case No. 1461-Y)
6. Stipulation (Case No. 1460-Y)
7. Stipulation (Case No. 1461-Y)
8. Minute Order of Court before Hon. Leon R. Yankwich, Tuesday, January 16, 1940 (Cases 1460-Y and 1461-Y)
9. Amended and Supplemental Answer (Case No. 1461-Y)
10. Minute Order (Case No. 1460-Y) [63]
11. Minute Order (Case No. 1461-Y)
12. Findings of Fact and Conclusions of Law (Case No. 1460-Y)
13. Findings of Fact and Conclusions of Law (Case No. 1461-Y)
14. Judgment (Cases Nos. 1460-Y and 1461-Y)

15. Notice of Appeal (Case No. 1460-Y)
16. Notice of Appeal (Case No. 1461-Y)
17. Stipulation for Consolidated Record on Appeal and Order attached (Cases Nos. 1460-Y and 1461-Y)
18. Stipulation for Order Extending Time for Filing Record on Appeal and Docketing the Action, and Order (Cases Nos. 1460-Y and 1461-Y)
19. This Designation of Record on Appeal
20. Reporter's Transcript.
21. Plaintiff's Exhibits "A" to "K" inclusive (Case No. 1460-Y)
22. Plaintiff's Exhibits 1 to 21 inclusive (Case No. 1461-Y)
23. Order Permitting Original Exhibits to be Sent to Circuit Court in lieu of Copies, on Appeal (Cases Nos. 1460-Y and 1461-Y)

Dated this 30th day of April, 1941.

WM. FLEET PALMER
United States Attorney
E. H. MITCHELL
Asst. United States Attorney
ARMOND MONROE JEWELL
Asst. United States Attorney
By ARMOND MONROE JEWELL
(Attorneys for Plaintiff)
MELVIN D. WILSON
JOSEPH D. PEELER
Attorneys for Defendant

[Endorsed]: Filed May 1, 1941. [64]

[Title of District Court and Cause—Nos. 1460-Y and 1461-Y.]

STIPULATION AND ORDER AS TO ORIGINAL PAPERS OR EXHIBITS

It is hereby stipulated by and between the respective parties, through their respective counsel that the Court may order the original stipulation, the exhibits, and reporter's transcript to the United States Circuit Court of Appeals for the Ninth Circuit in lieu of the copies thereof, such papers to be returned to the District Court upon the termination of the appellate proceedings.

Dated: April 30, 1941.

WM. FLEET PALMER
United States Attorney
E. H. MITCHELL
Asst. United States Attorney
ARMOND MONROE JEWELL
Asst. United States Attorney
By ARMOND MONROE JEWELL
Attorneys for Plaintiff
MELVIN D. WILSON
JOSEPH D. PEELER
Attorneys for Defendant. [65]

It Is So Ordered.

Dated: April 30, 1941.

LEON R. YANKWICH
Judge of the District Court

[Endorsed]: Filed May 1, 1941. [66]

[Title of District Court and Causes.]

CERTIFICATE OF CLERK

I, R. S. Zimmerman, Clerk of the District Court of the United States for the Southern District of California, do hereby certify that the foregoing pages, numbered from 1 to 66 inclusive, contain full, true and correct copies of the Bill of Complaint in each case; Answer in each case; Order Transferring case; Stipulation of Facts in each case; Order Consolidating Cases and Allowing Filing Amended and Supplemental Answer in Case No. 1461; Amended and Supplemental Answer in Case No. 1461; Decision of Court in each case; Findings of Fact and Conclusions of Law; Judgments; Notice of Appeal in each case; Stipulation and Order for Consolidated Record on Appeal; Stipulation and Order Extending Time to Docket Appeal; Stipulation Designating Record on Appeal and Stipulation and Order for Transmittal of Original Exhibits, Reporter's Transcript, etc., to the Circuit Court of Appeals, which together with the Original Exhibits and Reporter's Transcript of Proceedings transmitted herewith constitute the record on appeal to the United States Circuit Court of Appeals for the Ninth Circuit.

I do further certify that the clerk's fees for comparing, correcting and certifying the foregoing record amount to $10.10 which amount has been paid to me by Appellant.

Witness my hand and the seal of the District

Court of the United States for the Southern District of California, this 3rd day of May, A. D. 1941.

[Seal] R. S. ZIMMERMAN,
Clerk,
By: EDMUND L. SMITH
Deputy. [67]

[STATEMENT OF FACTS
Stipulated to in lieu of Reporter's Transcript]

(a) That these are suits in equity by the United States of America of a civil nature arising under the laws of the United States providing for internal revenue and the collection thereof, brought on September 9, 1938, at the direction of the Attorney General and begun and prosecuted with the sanction and at the request of the Commissioner of Internal Revenue to obtain relief for the appellee; and that the appellee has no clear, adequate, or complete remedy at law.

(b) That pursuant to and in accordance with an agreement between the Signal Gasoline Company, a California corporation, and the Signal Gasoline Corporation, a California corporation, dated May 1, 1924, all the assets of the Signal Gasoline Company were turned over to the Signal Gasoline Corporation for 400,000 shares of stock of the Signal Gasoline Corporation plus the assumption of "outstanding liabilities" not exceeding $51,076.80 (including all income taxes that may be due the United States Government to the date of the assign-

ment), and on September 11, 1924, the Signal Gasoline Company was dissolved; the 400,000 shares, received by the Signal Gasoline Company in exchange for its net assets, were distributed to its stockholders.

(c) That at all times herein mentioned the Signal Gasoline Company, Inc., a corporation now dissolved, was, prior to its dissolution, a holding company for the stock of the Signal Gasoline Corporation.

(d) That on July 31, 1928, the Signal Gasoline Company, Inc., owned 419,500 shares of the stock of the Signal Gasoline Corporation, which was 93.22% of the outstanding 450,005 shares of the Signal Gasoline Corporation; the balance of 30,505 shares of the stock outstanding of the Signal Gasoline Corporation (4.23%) was owned by individual stockholders of the Signal Gasoline Company, Inc.

(e) That on August 1, 1928, the appellant, Signal Oil and Gas Company, acquired all the assets of the Signal Gasoline Company, Inc., which, as noted above, included 93.22% of the stock of the Signal Gasoline Corporation, in exchange for stock of the Signal Oil and Gas Company.

(f) That on or about November 30, 1928, the appellant, Signal Oil and Gas Company, acquired the remaining 4.23% of the outstanding stock of the Signal Gasoline Corporation from the individual stockholders of the Signal Gasoline Company, Inc., by exchange for stock of the Signal Oil and Gas Company.

(g) That the Signal Gasoline Corporation was liquidated as of December 1, 1928, and all of its assets and liabilities were assigned in accordance with a certain instrument of conveyance and the Decree of Dissolution of the Superior Court. That Plaintiff's Exhibits 1 and 2 respectively, are true copies of the said instrument of conveyance and the Decree of Dissolution, and are attached hereto and made a part hereof.

(h) That the original 1923 income tax return of Signal Gasoline Company was filed by or on behalf of the Company on March 15, 1924, and an amended return for that year was filed on May 13, 1925. A tentative income tax return for Signal Gasoline Company for 1924 was filed March 16, 1925, and the final return for the year 1924 was filed on May 13, 1925.

(i) That on October 2, 1928, and again on December 28, 1929, the Commissioner of Internal Revenue duly addressed and mailed a letter to the Signal Gasoline Corporation setting forth certain transferee deficiencies; the letter of October 2, 1928, claiming a deficiency of $468.33 for 1923 to be due from Signal Gasoline Corporation as transferee of the assets of Signal Gasoline Company; the letter of December 28, 1929, claiming a deficiency of $2,672.53 for the period ended September 11, 1924, to be due from Signal Gasoline Corporation as transferee of the assets of Signal Gasoline Company.

(j) That thereafter petitions in the name of the Signal Gasoline Corporation were filed with the Board of Tax Appeals for a redetermination of the deficiencies proposed in the said letters dated October 2, 1928, and December 28, 1929; that the appeal from the deficiency proposed in the letter of October 2, 1928, was on November 19, 1928, docketed with the Board of Tax Appeals under No. 41532; that the appeal from the deficiency proposed in the letter of December 28, 1929, was on February 24, 1930, docketed with the Board of Tax Appeals under No. 47620. The petition numbered 47620 stated in its first paragraph that "The Petitioner is a dissolved Corporation acting through its statutory trustees * * *"; the verification on the petition numbered 47620 was signed by six persons, and this verification stated that these six persons were "* * * the statutory trustees of Signal Gasoline Corporation, a dissolved corporation * * *"; that the petition numbered 41532 and the petition numbered 47620 were each signed by Robert N. Miller and Melvin D. Wilson, as attorneys for the petitioners; that on February 16, 1932, the Board of Tax Appeals purported to affirm the rulings of the Commissioner of Internal Revenue in asserting the deficiencies appealed from in petitions numbered 41532 and 47620; that said decision of the Board of Tax appeals is contained in an opinion reported in 25 Board of Tax Appeals 532.

(k) That on September 10, 1932, the Commis-

sioner of Internal Revenue purported to assess the Signal Gasoline Corporation as a transferee of the Signal Gasoline Company, for the above described tax liabilities of the Signal Gasoline Company in the amounts and for the taxable periods as follows:

> For the taxable year 1923, $468.33 plus interest of $227.96. For the taxable period ended September 11, 1924, $2,672.53 plus interest of $1,200.70.

That attached hereto and made a part hereof is a true copy of Plaintiff's Exhibit J which is a true copy of the Assessment List of the Commissioner of Internal Revenue.

(l) Signal Gasoline Corporation filed its income tax return for the calendar year 1924 on or about May 13, 1925.

(m) On December 3, 1928, the Signal Gasoline Corporation signed and filed Form 872, which is entitled "Consent Fixing Period of Limitation upon Assessment of Income and Profits Tax"; that Plaintiff's Exhibit 4 is a true copy of the said form, and is attached hereto and made a part hereof.

(n) On December 28, 1929 the Commissioner of Internal Revenue addressed and mailed a letter to the Signal Gasoline Corporation; this letter proposed an assessment of additional tax liabilities against the Signal Gasoline Corporation on account of an alleged deficiency in its income tax for the period May 1, to December 31, 1924, in the amount of $14,137.05; that the said letter also proposed an

assessment of other additional tax liabilities for the calendar years 1925 and 1926.

(o) Under date of November 21, 1928, the Signal Gasoline Corporation executed a power of attorney to certain attorneys authorizing the said attorneys to represent the Signal Gasoline Corporation before the Treasury Department of the United States and the United States Board of Tax Appeals with reference to the tax liabilities of the Signal Gasoline Corporation for the calendar years 1924 and 1925; that attached hereto and made a part hereof is a true copy of Plaintiff's Exhibit 6 which is a true copy of said Power of Attorney.

(p) That under date of November 20, 1929, a power of attorney was executed whereby certain attorneys were authorized to represent Signal Gasoline Corporation, a dissolved corporation, before the Treasury Department and the Board of Tax Appeals in connection with the tax liabilities of the said corporation for the calendar years 1926 and 1927; that attached hereto is a true copy of Plaintiff's Exhibit 7 which is a true copy of said Power of Attorney.

(q) That on or about February 24, 1930, a petition was filed with the Board of Tax Appeals for a redetermination of the 1924, 1925 and 1926 deficiencies proposed in the Commissioner's letter dated December 28, 1929, above referred to; that said proceeding was therein given docket No. 47621; that said petition was filed under the name of the Sig-

nal Gasoline Corporation; the petition numbered 47621 stated in its first paragraph that: "The petitioner is a dissolved California corporation acting through its statutory trustees * * *"; the verification on the petition numbered 47621 was signed by six persons, and this verification stated that these six persons were "* * * the statutory trustees of Signal Gasoline Corporation, a dissolved corporation * * *"; that the petition numbered 47621 was signed by Robert N. Miller and Melvin D. Wilson as attorneys for the petitioners; that on March 15, 1932, the Board of Tax Appeals purported to affirm the rulings of the Commissioner of Internal Revenue in asserting the deficiencies appealed from in petition numbered 47621; that said decision of the Board of Tax Appeals is contained in an opinion reported in 25 Board of Tax Appeals 861.

(r) On October 1, 1932, the Commissioner of Internal Revenue purported to assess the Signal Gasoline Corporation for its tax deficiency for the calendar year 1924 in the principal amount of $14,137.05, plus interest of $6,080.77; that attached hereto and made a part hereof is a true copy of Plaintiff's Exhibit 9 which is a true copy of the Assessment list of the Commissioner of Internal Revenue.

(s) That by reason of the dissolution of the Signal Gasoline Corporation and the disbursement of all of its assets to its statutory trustees, as above set forth, the Signal Gasoline Corporation was and

is left without any money, assets or property of any kind with which to pay the said taxes and interest claimed herein by the United States.

(t) That the assets which were acquired by the appellant, Signal Oil and Gas Company, as sole stockholder of the Signal Gasoline Corporation, as heretofore shown, were far in excess of the taxes and interest prayed for in the complaints herein.

(u) That due demand for the payment of the taxes and interest prayed for in the complaints herein has been made upon the Signal Oil and Gas Company but no portion thereof has been paid.

(v) That at all times herein mentioned and considered substantially the same persons were officers and directors or statutory trustees of the Signal Gasoline Corporation as were the officers and directors of the Signal Oil and Gas Company and officers and directors of the Signal Gasoline Company.

(w) That in the proceedings before the Board of Tax Appeals under docket numbers 41532, 47620 and 47621, no substitution of parties was ever made and no motion for such substitution was ever made by either of the parties.

(x) A protest against a proposed deficiency for 1927 income taxes of Signal Gasoline Corporation was signed about November 20, 1929. This protest was signed "Signal Gasoline Corporation, By S. B. Mosher". At the left of the said signature, five other trustees of the dissolved corporation signed

their names. The protest was verified by Melvin D. Wilson, one of the attorneys in fact and in law, who stated that he had verified it for the reason that when "the statutory trustees" signed the protest, they neglected to acknowledge it before a notary public.

An offer to compromise the taxes here involved, acknowledged October 21, 1932, was filed shortly thereafter. It was signed "Signal Gasoline Corporation, By S. B. Mosher, H. M. Mosher, O. W. March, R. H. Green, C. LaV. Larzelere". The acknowledgment stated that the above named persons were the statutory trustees of Signal Gasoline Corporation, a dissolved corporation. In the body of the offer, it was stated that Signal Gasoline Corporation was dissolved December 12, 1928.

A similar offer, acknowledged January 23, 1933, and filed shortly thereafter, stated that Signal Gasoline Corporation was dissolved December 12, 1928. It was signed "Signal Gasoline Corporation, By Melvin D. Wilson, Attorney in Fact". In the acknowledgment, it was stated that Signal Gasoline Corporation was a dissolved corporation.

(y) Except for the matters covered in this record, no other correspondence with the Commissioner or Collector of Internal Revenue was filed by or on behalf of the Signal Gasoline Company or the Signal Gasoline Corporation after their dissolution, excepting:

1. That on January 20, 1932, a letter to the Commissioner was written and signed "Signal Gas-

oline Corporation, By J. H. Rounsavell, Comptroller", advising the Commissioner to change his records so that all correspondence relative to the income tax matters of Signal Gasoline Corporation for 1924 to 1928 inclusive would be sent to 1200 Signal Oil Building, 811 West Seventh Street, Los Angeles, California.

2. On January 20, 1932, a letter to the Commissioner signed "Signal Gasoline Company, By J. H. Rounsavell, Comptroller", was mailed, advising the Commissioner to change his records so that all correspondence pertaining to the income liability of Signal Gasoline Company for 1922 to 1924 inclusive would be sent to 1200 Signal Oil Building, 811 West Seventh Street, Los Angeles, California.

3. On January 20, 1932, a letter to the Commissioner, signed by "Signal Gasoline Company, Inc. by J. H. Rounsavell, Comptroller" was mailed, advising the commissioner to change his records so that all correspondence pertaining to the income tax liability of Signal Gasoline Company for 1925, 1926, 1927 and 1928 inclusive would be sent to 1200 Signal Oil Building, 811 West Seventh Street, Los Angeles, California.

4. On July 27, 1931, a letter signed "Signal Gasoline Corporation, by J. H. Rounsavell, Comptroller" was mailed to the Collector at Los Angeles, California, stating that there was pending before the United States Board of Tax Appeals the question of whether Signal Gasoline Corporation was

liable for the 1923 income tax liability of Signal Gasoline Company.

(z) That no assessment was ever made against the Signal Oil and Gas Company for the 1923 and 1924 tax liabilities of the Signal Gasoline Company; that no assessment was ever made against the Signal Oil and Gas Company for the tax liabilities due from the Signal Gasoline Corporation for the year 1924; that no assessment was ever made against the Signal Gasoline Company for the said 1924 tax liability of the Signal Gasoline Company; that an assessment against the Signal Gasoline Company was made on July 3, 1931, in the amount of $468.33 plus interest for its said tax liability for the calendar year 1923.

(aa) On May 13, 1929, a corporation income tax return for 1928 was filed with the Collector of Internal Revenue at Los Angeles, California on behalf of the Signal Gasoline Corporation and was signed by S. B. Mosher, as President, and O. W. March, as Treasurer of the said corporation. In said return it was stated in Affiliation Schedule No. 3 thereof that the Signal Gasoline Corporation had been dissolved in December of 1928.

(bb) In a Revenue Agent's report, dated August 26, 1930, it was stated that the Signal Gasoline Corporation had distributed all of its assets to its sole stockholder, the Signal Oil and Gas Company, upon its dissolution in December, 1928. In a letter dated March 30, 1931 from the Commissioner of Internal Revenue and addressed to the

Signal Gasoline Corporation, which letter was the 60-day letter proposing additional taxes for the year 1928, it was stated that the Signal Gasoline Corporation had been dissolved in December, 1928.

PLAINTIFF'S EXHIBIT 1
SIGNAL GASOLINE CORPORATION
NOTICE RE: CONVEYANCE OF ASSETS

Know All Men By These Presents:

That whereas, on the 12th day of December, 1928, The Superior Court of the State of California in and for the County of Los Angeles made and filed its decree dissolving the Signal Gasoline Corporation, which decree was, on the 13th day of December, 1928 entered in Book 701 at Page 165 of Judgments, Records of said County of Los Angeles, and whereas, in the aforesaid Decree it was ordered and decreed that S. B. Mosher, H. M. Mosher, O. W. March, Ross McCollum, C. LaV. Larzelere and R. H. Green were entitled to be, and were by the Court therein appointed Trustees for the stockholders of said corporation, with power and direction to settle all the affairs of said corporation and to distribute and convey all of the property of said corporation to the stockholders thereof a copy of which decree is hereunder annexed and made a part hereof, and whereas the Signal Oil and Gas Company, a Delaware corporation, is the owner and holder of all the issued and outstanding stock of

said Signal Gasoline Corporation and as such is entitled to distribution of all of the property of said Signal Gasoline Corporation; Now therefore, in consideration of the premises S. B. Mosher, H. M. Mosher, O. W. March, Ross McCollum, C. LaV. Larzelere and E. H. Green, as Trustees for the stockholders of said Signal Gasoline Corporation, a dissolved corporation, and also in their individual capacities, do hereby assign, transfer, grant, convey, deliver and distribute to said Signal Oil and Gas Company, a Delaware corporation, all of the assets, business and property as a whole and of every kind, character and description, both tangible and intangible, legal and equitable and wherever situated, including all real property and all interests therein situate in the State of California and elsewhere, possessed by said dissolved corporation at the time of its dissolution, including all cash on hand and all bills and accounts receivable of said dissolved corporation from whomever due and wheresoever evidences thereof, if any, may be held, and all contract rights, rights of action, vouchers and things in action, and without any limitation or exception whatsoever, and subject to all outstanding obligations and liabilities thereon, and subject to the payment of income taxes that may be due to the United States Government covering operations of said dissolved corporation during the current year and all sums that may be found due covering income taxes for previous years. We further

give to said Signal Oil and Gas Company, its successors and assigns, both power and authority for its own use and benefit, but at its own cost, to take all legal measures which may be proper and necessary for the complete recovery of any of the property hereby assigned, and in its own name to prosecute and withdraw any suit at law or equity therefor. The transfer of the foregoing property shall take effect as of the date of this instrument, to-wit: the 14th day of December, 1928.

In Witness Whereof, we have executed this instrument in the manner hereinafter appearing, in the capacity and pursuant to the authority above related and also in our individual capacities, this 14th day of December, 1928.

R. H. GREEN
C. LaV. LARZELERE
O. W. MARCH
ROSS McCOLLUM
S. B. MOSHER
H. M. MOSHER

as Trustees for the Signal Gasoline Corporation, a Dissolved Corporation.

R. H. GREEN
C. LaV. LARZELERE
O. W. MARCH
ROSS McCOLLUM
S. B. MOSHER
H. M. MOSHER

as individuals.

(Subscribed and sworn to before May E. Martin, Notary Public, December 14, 1928.)

[Endorsed]: U. S. Exhibit No. 1. Filed 1/16/40. R. S. Zimmerman, Clerk. By Louis J. Somers, Deputy Clerk.

PLAINTIFF'S EXHIBIT 2

In the Superior Court of the State of California, in and for the County of Los Angeles

No. 263815

In the Matter of the Application of

SIGNAL GASOLINE CORPORATION, a corporation, for Dissolution.

DECREE OF DISSOLUTION

The voluntary application for dissolution of the Signal Gasoline Corporation, a domestic corporation, coming on regularly this day for hearing and determination, the Court finds: 1. That on October 19, 1928 in accordance with the order of the Judge of this Court, the said Signal Gasoline Corporation filed with the Clerk of this Court its application for its dissolution as a corporation. 2. That in accordance with the order of a Judge of this Court the Clerk of said Court has given thirty days' notice of said application for dissolution, by publication in the Los Angeles Daily Journal, a newspaper of general circulation printed and pub-

lished in the said County of Los Angeles, which thirty days' notice which said publication thereof was completed and expired on November 27, 1938. 3. That no objection to said application for dissolution has at any time been filed. 4. All allegations and statements in said application for dissolution made are true and to this court, by this evidence introduced herein, have been shown so to be. 5. And it further appears to the Court from evidence introduced herein that the Board of Directors of said corporation under its Articles of Incorporation consisted of six (6) members and does now consist of six (6) members, namely:

S. B. MOSHER
O. W. MARCH
ROSS McCOLLUM
H. M. MOSHER
C. LaV. LARZELERE
R. H. GREEN

Wherefore, it is Ordered, Adjudged and Decreed, that said Corporation, the Signal Gasoline Corporation be, and the same is, and is hereby declared to be dissolved. It is further Ordered and Decreed that said S. B. Mosher, H. M. Mosher, O. W. March, Ross McCollum, C. LaV. Larzelere and R. H. Green are entitled to be, and are by the Court herein appointed, trustees for the stockholders of said corporation, with power and direction to settle all the affairs of said corporation, and to distribute and convey all the property of said corporation to each of said stockholders, in proportion to the number of

shares owned and held by said stockholders when said distribution and conveyance shall be made.

Done in open Court this 12th day of December 1928.

(Signed) MARSHALL McCOMB,
Judge.

#1816 Copy of original recorded at request of Signal Oil and Gas Company, 503 Roosevelt Building, Los Angeles, Calif., March 6, 1929 at 58 minutes past 2 p. m.

Copyist #61. Compared.

C. L. LOGAN,
Recorder,
By W. WHITNEY,
Deputy.

[Endorsed]: U. S. Exhibit No. 2. Filed 1/16/40. R. S. Zimmerman, Clerk. By Louis J. Somers, Deputy Clerk.

PLAINTIFF'S EXHIBIT "J"

ASSESSMENT CERTIFICATE
COMMISSIONER'S ASSESSMENT LIST

6th District of California
Month September 2 Year 1932

Additional Assessments made by Commissioner:

Personal	$ 70,966.13
Corporation	4,933.98
Total Assessments	75,900.11

I hereby certify that I have made inquiries, determinations, and assessments of taxes, penalties,

etc., of the above classification specified in these lists, and find that the amounts of taxes, penalties, etc., stated as corrected and as specified in the supplementary pages of this list made by me are due from the individuals, firms, and corporations opposite whose names such amounts are placed, and that the amount chargeable to the collector is as above.

Dated at Washington, D. C.

Office of Commissioner of Internal Revenue, September 10, 1932

(Signed) DAVID BURNET
Commissioner of Internal Revenue

ASSESSMENT LIST Page No. 0

District 6th California, Income Tax, List September 2 1932

	Old Balance	Date	Debit	Credit	New Balance	Remarks
1. Signal Gasoline Corp		Transferee	468.33			1923 2105
505 Roosevelt Building		Int to 9-10-32	227.96		696.29	274B & 280 1
Los Angeles Calif		Transferor Signal Gasoline Co 6th Calif Dist				OL 10-2-28
Sept 01 C#2			No Assessment			
2. Signal Gasoline Corp		Transferee	2672.53		3873.23	1924 2105
505 Roosevelt Building		Int to 9-10-32	1200.70			274B & 280 2
Los Angeles Calif		Transferor Signal Gasoline Co. 6th Calif Dist				OL 12-28-29
Sept 02 C#2			No Assessment			

[Endorsed]: U. S. Exhibit No. J. Filed 1/16/40. R. S. Zimmerman, Clerk. By Louis J. Somers, Deputy Clerk.

PLAINTIFF'S EXHIBIT 4

CONSENT FIXING PERIOD OF LIMITATION UPON ASSESSMENT OF INCOME AND PROFITS TAX

For Taxable Years Ended Prior to January 1, 1926.

November 21, 1928

In pursuance of the provisions of existing Internal Revenue Laws Signal Gasoline Corporation, a taxpayer of Los Angeles, California, and the Commissioner of Internal Revenue hereby consent and agree as follows:

That the amount of any income, excess-profits, or war-profits taxes due under any return made by or on behalf of the above-named taxpayer for the year (or years) 1924 and 1925, under existing acts, or under prior revenue acts, may be assessed at any time on or before December 31, 1929, except that, if a notice of a deficiency in tax is sent to said taxpayer by registered mail on or before said date, then the time for making any assessment as aforesaid shall be extended beyond the said date by the number of days during which the Commissioner is prohibited from making an assessment and for sixty days thereafter.

[Seal] SIGNAL GASOLINE CORPORATION
S. B. MOSHER, Pres.
Taxpayer

By.....

D. H. BLAIR Commissioner

If this consent is executed on behalf of a corporation, it must be signed by such officer or officers of the corporation as are empowered under the laws of the State in which the corporation is located to sign for the corporation, in addition to which, the seal, if any, of the corporation must be affixed. Where the corporation has no seal, the consent must be accompanied by a certified copy of the resolution passed by the Board of Directors, giving the officer authority to sign the consent.

(U. S. Board of Tax Appeals Div. 8 Docket 47621—Admitted in Evidence June 3 1931 Petitioner's Exhibit "A")

(Received Dec. 3 1928 Office of Head Audit Review Division)

[Endorsed]: U. S. Exhibit No. 4. Filed 1/16/40. R. S. Zimmerman, Clerk. By Louis J. Somers, Deputy Clerk.

PLAINTIFF'S EXHIBIT 6

Power of Attorney

Los Angeles, California,
November 21, 1928.

Commissioner of Internal Revenue,
Washington, D. C.
Sir:—

The undersigned corporation, Signal Gasoline Corporation, a corporation duly organized and existing under the laws of the State of California, with its principal place of business at Los Ange-

les, California, does hereby make, constitute and appoint Dana Latham and Melvin D. Wilson, of Miller, Chevalier & Latham, 819 Title Insurance Bldg., Los Angeles, California; Robert N. Miller and Ward Loveless, of Miller & Chevalier, 922 Southern Bldg., Washington, D. C.; Walker S. Clute, Roosevelt Bldg., Los Angeles, California, and Roger F. White, 804 Hellman Bank Bldg., Los Angeles, California, and each of them, its true and lawful attorneys, for it and in its name to represent it before the Treasury Department of the United States, any bureau or official thereof, and the United States Board of Tax Appeals, in all matters pertaining to the determination, assessment, collection or payment of any taxes under the laws of the United States and to all claims for abatement, refund or credit based on the assessment or payment of any such taxes; and, without limiting the foregoing powers, to examine and to request and receive copies of all returns, claims and other documents; to receive and receipt, in its behalf, for all checks and warrants made by the United States on account of any refunds; and generally to do, execute and perform all acts and things necessary or convenient in the premises (including authority to verify petitions to the said Board of Tax Appeals), with full power of substitution and revocation, hereby ratifying and confirming all that its attorneys and substitutes from time to time shall do or cause to be done by virtue thereof, and hereby expressly revoking all previous Powers of Attorney given by said corporation.

The foregoing powers shall apply to each of the transactions heretofore directed or authorized, with respect to taxes for the years 1924 and 1925.

Respectfully,
(Seal) SIGNAL GASOLINE
CORPORATION,
By S. B. MOSHER,
By O. W. MARCH.

State of California,
County of Los Angeles—ss.

On this 23 day of November, A. D. 1928, personally before me appeared the above named S. B. Mosher and O. W. March, to me known to be the parties who executed the foregoing Power of Attorney, who, first being duly sworn, stated: that they are the President and Secretary respectively, of the above-named corporation; that they signed, sealed and delivered the above instrument, pursuant to authority duly conferred upon them in that behalf, as the free and voluntary act of the said corporation, for the uses and purposes therein set forth.

In Witness whereof, I have hereunto set my hand and affixed my official seal this 23 day of November, A. D. 1928.

(Seal) MARY E. MARTIN,
Notary Public, in and for the County of Los Angeles, State of California.

[Endorsed]: U. S. Exhibit No. 6. Filed 1-16-40. R. S. Zimmerman, Clerk. By Louis J. Somers, Deputy Clerk.

PLAINTIFF'S EXHIBIT 7

Power of Attorney

Los Angeles, California.
November 20, 1929.

Commissioner of Internal Revenue,
Washington, D. C.
Sir:—

The undersigned corporation, Signal Gasoline Corporation, a dissolved California corporation, through its statutory trustees whose principal place of business is at 505 Roosevelt Building, Los Angeles, California, does hereby make, constitute and appoint the law firm of Miller, Chevalier, Peeler & Wilson, 819 Title Insurance Bldg., Los Angeles, California, particularly Joseph D. Peeler and Melvin D. Wilson of that firm; and the law firm of Miller & Chevalier, 922 Southern Building, Washington, D. C., particularly Robert N. Miller, Ward Loveless, and J. Robert Sherrod of that firm; Walker S. Clute, Roosevelt Bldg., Los Angeles, California; and Roger F. White, Hellman Bank Bldg., Los Angeles, California, and each of them its true and lawful attorneys for it and in its name to represent it before the Treasury Department of the United States, any bureau or official thereof, and the United States Board of Tax Appeals, in all matters pertaining to the determination, assessment, collection or payment of any taxes under the laws of the United States and to all claims for abatement, refund or credit based on the assessment or

payment of any such taxes; and, without limiting the foregoing powers, to examine and to request and receive copies of all returns, claims and other documents; and generally to do, execute and perform all acts and things necessary or convenient in the premises (including authority to verify petitions to the said Board of Tax Appeals), with full power of substitution and revocation, hereby ratifying and confirming all that its attorneys and substitutes from time to time shall do or cause to be done by virtue thereof, and hereby expressly revoking all previous Powers of Attorney given by said corporation.

The foregoing powers shall apply to each of the transactions heretofore directed or authorized, with respect to taxes for the years 1926 and 1927.

Respectfully,
SIGNAL GASOLINE
CORPORATION,
By S. B. MOSHER.

R. H. GREEN
O. W. MARCH
ROSS. McCOLLUM
H. M. MOSHER
C. L. LARZALERE

State of California,
County of Los Angeles—ss.

On this 23 day of November, A. D. 1929, personally before me appeared the above named to me known to be the parties who executed the forego-

ing Power of Attorney, who, first being duly sworn, stated: that they are the statutory trustees of the above-named dissolved corporation; that they signed, sealed and delivered the above instrument, pursuant to authority duly conferred upon them in that behalf, as the free and voluntary act of the said dissolved corporation, for the uses and purposes therein set forth.

In witness whereof, I have hereunto set my hand and affixed my official seal this 23 day of November, A. D. 1929.

(Seal) MARY E. MARTIN,
Notary Public, in and for the County of Los Angeles, State of California.

[Endorsed]: U. S. Exhibit No. 7. Filed 1-16-40. R. S. Zimmerman, Clerk. By Louis J. Somers, Deputy Clerk.

PLAINTIFF'S EXHIBIT 9

Assessment Certificate

Commissioner's Assessment List

6th District of California. Month October 1 Year 1932.

Additional Assessments made by Commissioner:

Personal—$39706.99.

Corporation—$104301.15.

Total Assessments—$144008.14.

I hereby certify that I have made inquiries, determinations, and assessments of taxes, penalties, etc., of the above classification specified in these

lists, and find that the amounts of taxes, penalties, etc., stated as corrected and as specified in the supplementary pages of this list made by me are due from the individuals, firms, and corporations opposite whose names such amounts are placed, and that the amount chargeable to the collector is as above.

Dated at Washington, D. C., Office of Commissioner of Internal Revenue, October 1, 1932.

(Signed) DAVID BURNET,
Commissioner of Internal Revenue.

ASSESSMENT LIST Page No. 0

District 6th California, Income Tax List October #1 1932

		Old Balance Date	Debit	Credit	New Balance	Remarks
0	Signal Gasoline Corp 505 Roosevelt Bldg Los Angeles Cal	Int to 10/1/32	14137.05 6080.77		20217.82	1924 5/1-12/31 403117 274B WVR RAR 0 OL 12/28/29
	Oct 00 C #1					
	Signal Gasoline Corp.		19340.18		26933.72	1925 402913
1	505 Roosevelt Bldg Los Angeles Cal	Int to 10/1/32	7593.54			274B RAR WVR OL 12/28/29 1
	Oct 01 C #1					
	Signal Gasoline Corp		40804.19		54376.89	1926 401212
2	505 Roosevelt Bldg Los Angeles Cal	Int to 10/1/32	13572.70			274B RAR 2 OL 12/28/29

Oct 02 C #1

[Endorsed]: U. S. Exhibit No. 9. Filed 1-16-40. R. S. Zimmerman, Clerk. By Louis J. Somers, Deputy Clerk.

[Endorsed]: No. 9813. United States Circuit Court of Appeals for the Ninth Circuit. Signal Oil and Gas Company, a Corporation, Appellant, vs. United States of America, Appellee. Transcript of Record Upon Appeals From the District Court of the United States for the Southern District of California, Central Division.

Filed May 6, 1941.

PAUL P. O'BRIEN,

Clerk of the United States Circuit Court of Appeals for the Ninth Circuit.

United States Circuit Court of Appeals for the Ninth Circuit

No. 9813

SIGNAL OIL AND GAS COMPANY, a Corporation, Appellant,

vs.

UNITED STATES OF AMERICA, Appellee.

SIGNAL OIL AND GAS COMPANY, a Corporation, Appellant,

vs.

UNITED STATES OF AMERICA, Appellee.

STATEMENT OF POINTS UPON WHICH APPELLANT INTENDS TO RELY ON THE APPEAL.

1. There was no evidence introduced at the trial showing that the taxes sued on were due from anyone. The alleged assessments relied on by the Appellee for that purpose were void and prove nothing, having been purportedly made long after the corporations against which they were supposed to have been made had been dissolved and utterly destroyed by their dissolution. Said alleged assessments were based upon alleged proceedings in the Board of Tax Appeals wherein the Appellee was guilty of laches in that it did not move for a dis-

missal or substitution of the parties petitioner although long having knowledge that the petitioners had been dissolved and destroyed by their dissolutions.

2. The suits by Appellee were barred by the statute of limitations as they were not brought within four years of the filing of the returns of the corporations whose taxes were involved and no assessment was made against the Appellant, but the Appellee was relying upon a six-year period within which to sue Appellant after alleged assessments against a prior transferee, but the alleged assessments against the prior transferee were invalid for the reason stated in Point 1, and even if the assessments against the prior transferee had been valid, they would not give Appellee six years within which to sue subsequent transferees.

3. Appellant is not estopped from asserting the bar of the statute of limitations, Appellee having at all times been in possession of all the material facts and having initially made an error of law which error misled the Appellant into further errors of law, if appellant made any errors of law, but estoppel does not arise from errors or mutual errors of law.

4. The judgments against Appellants should be reversed.

Dated: May 1, 1941.

MELVIN D. WILSON,
JOSEPH D. PEELER,
By M. D. W.

819 Title Insurance Building, Los Angeles, California, Counsel for Appellant.

Received copy of the within this 1 day of May, 1941.

WM. FLEET PALMER,
U. S. Atty.
By ARMOND MONROE JEWELL,
Attorney for Appellee.

[Endorsed]: Filed May 6, 1941. Paul P. O'Brien, Clerk.

[Title of Circuit Court of Appeals and Cause.]

STIPULATION DESIGNATING THOSE PORTIONS OF THE RECORD ON APPEAL DEEMED MATERIAL AND WHICH ARE THEREFORE TO BE PRINTED.

Pursuant to Rule 19, Subdivision 6, of the Rules of Court of the United States Circuit Court of Appeals for the Ninth Circuit, It Is Hereby Stipulated by and between the respective parties hereto, through their respective counsel, that the following are deemed the material portions of the record on appeal in the above entitled cases and which are therefore to be printed:

1. Order Transferring Case Pursuant to Rule 19, dated February 8, 1939 (Case 1461 R.J.) (R. p. 23.)

2. Complaint (Case 1460-Y) (R. p. 2 to p. 6 inc.)

3. Complaint (Case 1461-Y) (R. p. 7 to p. 11 inc.)

4. Answer (Case 1460-Y) (R. p. 12 to p. 17 inc.)

5. Answer (Case 1461-Y) (R. p. 18 to p. 22 inc.)

6. Stipulation (Case 1460-Y) (R. p. 24 to p. 29 inc.)

7. Stipulation (Case 1461-Y) (R. p. 30 to p. 36 inc.)

8. Minute Order of Court before Hon. Leon R. Yankwich, Tuesday, January 16, 1940 (Cases 1460-Y and 1461-Y) (R. p. 37)

9. Amended and Supplemental Answer (Case No. 1461-Y) (R. p. 38 to p. 40 inc.)

10. Minute Order (Case No. 1460-Y) (R. pp. 41, 42)

11. Minute Order (Case 1461-Y) (R. pp. 43, 44)

12. Findings of Fact and Conclusions of Law (Cases 1460-Y and 1461-Y) (R. p. 45 to p. 54 Inc.)

13. Judgment (Cases 1460-Y and 1461-Y) (R. pp. 55, 56)

14. Notice of Appeal (Case 1460-Y) (R. p. 57)

15. Notice of Appeal (Case 1461-Y) (R. p. 58)

16. Stipulation for Consolidated Record on Ap-

peal and Order attached (Cases 1460-Y and 1461-Y) (R. pp. 59, 60)

17. Stipulation for Order Extending Time for Filing Record on Appeal and Docketing the Action, and Order (Cases 1460-Y and 1461-Y) (R. pp. 61, 62)

18. Designation of Record on Appeal (Cases 1460-Y and 1461-Y) (R. pp. 63, 64)

19. Order Permitting Original Exhibits to be Sent to Circuit Court in lieu of Copies on Appeal (Cases 1460-Y and 1461-Y) (R. pp. 65, 66)

It is further stipulated by and between the respective parties hereto, through their respective counsel, that in lieu of printing the material portions of the admissions in the pleadings, the written stipulations of fact, the documents admitted into evidence, and the verbal stipulations contained in the transcript of record, that for the purpose of this apeal, the following statement may and should

be printed as a summary of the facts adduced therefrom:

Dated: May 2, 1941.

MELVIN D. WILSON,
JOSEPH D. PEELER.
Attorneys for Apellant.

WM. FLEET PALMER,
United States Attorney.
E. H. MITCHELL,
Asst. United States Attorney.
ARMOND MONROE JEWELL,
Asst. United States Attorney.
By ARMOND MONROE JEWELL,
Attorneys for Appellee.

Approved:

LEON R. YANKWICH,
District Judge.

[Endorsed]: Filed May 6, 1941. Paul P. O'Brien, Clerk.

No. 9813.

IN THE

United States Circuit Court of Appeals

FOR THE NINTH CIRCUIT

SIGNAL OIL AND GAS COMPANY, a corporation,

Appellant,

vs.

UNITED STATES OF AMERICA,

Appellee.

BRIEF FOR APPELLANT.

MELVIN D. WILSON,
819 Title Insurance Building, Los Angeles,
Attorney for Appellant.

Parker & Baird Company, Law Printers, Los Angeles.

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No. 9813.

IN THE

United States Circuit Court of Appeals

FOR THE NINTH CIRCUIT

SIGNAL OIL AND GAS COMPANY, a corporation,

Appellant,

vs.

UNITED STATES OF AMERICA,

Appellee.

BRIEF FOR APPELLANT.

Opinion Below.

The opinion of the District Court of the United States for the Southern District of California, Central Division [R. 45 to 47] is unreported.

Jurisdiction.

These appeals involve Federal income tax for the years 1923 and 1924 and were taken from judgments of the District Court of the United States for the Southern District of California, Central Division, entered December 26, 1940. [R. 61 to 63.] The notices of appeal were filed March 20, 1941 [R. 64 to 65] pursuant to provisions of Section 128 of the Judicial Code. The District Court took jurisdiction under the provisions of Section 24 (1) of the Judicial Code. [R. 2.]

There were two separate proceedings below which were consolidated for trial [R. 42] and which have been con-

solidated for purposes of this appeal. [R. 65.] One proceeding, Case No. 1460-Y, involved a suit by the appellee against the appellant in equity under the trust fund theory for the 1923 and 1924 Federal income tax of Signal Gasoline Company [R. 2 to 9], while the other involved a suit in equity by the appellee against the appellant under the trust fund theory for Federal income taxes for the year 1924 of Signal Gasoline Corporation. [R. 9 to 15.]

The appellant, Signal Oil and Gas Company, is a corporation organized under the laws of the State of Delaware, and has its principal place of business at Los Angeles, California.

Questions Presented.

1. Whether any taxes were due from the Signal Gasoline Company or Signal Gasoline Corporation, the only evidence thereof being purported assessments made in the name of Signal Gasoline Corporation years after it had been dissolved and, by virtue of California law, completely destroyed.

2. Assuming without conceding that the said alleged assessments were valid, were the suits against appellant barred by the statute of limitations where appellant in each case was the transferee of a transferee of the corporation whose taxes are alleged to be due?

3. If the suits are *prima facie* barred by the statute of limitations, is appellant estopped from asserting the bar of the statute of limitations where the appellee had all the facts and simply made errors of law?

Statutes Involved.

The statutes involved are set out in the appendix.

Statement.

The pertinent facts are set out in the record [pp. 72 to 83 incl.] and the exhibits set out in the record [pp. 83 to 100 incl.]. The facts in Case No. 1460-Y may be briefly stated as follows:

On May 1, 1924, Signal Gasoline Company transferred all its assets to Signal Gasoline Corporation in exchange for the assumption of outstanding liabilities not exceeding $51,076.80 including all income taxes that might be due the Government as of the date of the assignment, plus 400,000 shares of the stock of Signal Gasoline Corporation. On September 11, 1924, Signal Gasoline Company was dissolved and distributed its assets, being the 400,000 shares of stock of Signal Gasoline Corporation, to its stockholders. [R. 72 to 73.]

The appellant, Signal Oil and Gas Company, was organized under the laws of the State of Delaware in 1928 and by November 30, 1928, had acquired 100% of the stock of Signal Gasoline Corporation in exchange for its own stock. [R. 73.]

Signal Gasoline Corporation was liquidated as of December 1st, 1928, and all its assets and liabilities were assigned in accordance with a certain instrument of conveyance and the Decree of Dissolution of the Superior Court. [R. 74.] The Decree of Dissolution set forth that S. B. Mosher, O. W. March, Ross McCollum, H. M. Mosher, C. Lav. Larzalere and R. H. Green were the members of the Board of Directors of the Signal Gasoline Corporation. They were appointed by the Court as trustees for the stockholders and creditors of the corporation, with power and direction to settle all the affairs of the corporation and to distribute

and convey all the property of said corporation to each of said stockholders in proportion to the number of shares owned and held by said stockholders when said distribution and conveyance was made. [Plaintiff's Exhibit 2; R. 87-88.] On December 14, 1928, the said trustees of Signal Gasoline Corporation executed a notice re conveyance of assets which recited the court decree and the appointment of the statutory trustees, and which recited that the Signal Oil and Gas Company was the owner of all the outstanding stock of Signal Gasoline Corporation and was entitled to the distribution of all the assets of that company. Said notice did assign to the Signal Oil and Gas Company all the assets of the Signal Gasoline Corporation subject to all the outstanding liabilities and to the payment of income taxes that might be due to the Government covering operations of the dissolved corporation during the current year, and all sums that might be found due covering income taxes for previous years. [Plaintiff's Exhibit 2; R. 83-84.]

The original income tax return for 1923 of Signal Gasoline Company was filed on behalf of that company on March 15, 1924, and an amended return for that year was filed May 13, 1925. A tentative return for 1924 was filed March 16, 1925, and the final return for 1924 was filed May 13, 1925. [R. 74.]

On October 2, 1928, and again on December 28, 1929, the Commissioner of Internal Revenue addressed and mailed a letter to the Signal Gasoline Corporation setting

forth certain transferee deficiencies; the letter of October 2, 1928, claiming a deficiency of $468.33 for 1923 to be due from Signal Gasoline Corporation as transferee of the assets of Signal Gasoline Company; the letter of December 28, 1929, claiming a deficiency of $2672.53 for the period ended December 11, 1924, to be due from Signal Gasoline Corporation as transferee of the assets of Signal Gasoline Company. [R. 74.]

On November 19, 1928, Signal Gasoline Corporation filed with the United States Board of Tax Appeals an appeal from the deficiency proposed in the letter of October 2, 1928. This petition was docketed with the Board under No. 41532. [R. 75.]

On February 24, 1930, a petition was filed in the name of Signal Gasoline Corporation, appealing from the deficiency proposed in the letter of December 28, 1929. This petition was docketed with the United States Board of Tax Appeals under No. 47620. This petition, in its first paragraph stated that: "The petitioner is a dissolved corporation acting through its statutory trustees * * *". The verification of the petition was signed by the six persons who had been appointed by the Court as statutory trustees of Signal Gasoline Corporation, and the verification stated that these six persons were "* * * the statutory trustees of Signal Gasoline Corporation, a dissolved corporation * * *". [R. 75.]

Both of the petitions mentioned above were signed by Robert N. Miller and Melvin D. Wilson as attorneys for the petitioners. [R. 75.]

These matters were pending before the Board of Tax Appeals from November 19, 1928, and February 24, 1930, respectively, until February 16, 1932. [R. 75.] No substitution of parties was ever made and no motion of such substitution was ever made by either of the parties though the Commissioner of Internal Revenue was informed of the dissolution of Signal Gasoline Corporation in December of 1928 as follows [R. 79]:

1. On May 13, 1929, a corporation income tax return for 1928 was filed with the Collector of Internal Revenue at Los Angeles, California, on behalf of the Signal Gasoline Corporation. In said return it was stated in affiliation schedule No. 3 thereof, that the Signal Gasoline Corporation had been dissolved in December of 1928. The return was signed by S. B. Mosher as president, and O. W. March as treasurer. [R. 82.]

2. On November 20, 1929, a power of attorney was executed whereby certain attorneys were authorized to represent Signal Gasoline Corporation, a dissolved corporation, before the Treasury Department in connection with the tax liabilities of said corporation for the calendar years 1926 and 1927. Said power of attorney stated that the Signal Gasoline Corporation was a dissolved California corporation acting through its statutory trustees. It was signed by Signal Gasoline Corporation, by S. B. Mosher and five other persons, and the verification stated that the persons who had signed it were the statutory trustees of the above named dissolved corporation. [Plaintiff's Exhibit 7; R. 95-96.]

3. On February 24, 1930, the petition to the Board of Tax Appeals was filed as indicated above, stating that Sig-

nal Gasoline Corporation was a dissolved corporation acting through its statutory trustees, and the verification was signed by six persons who stated that they were the statutory trustees of Signal Gasoline Corporation, a dissolved corporation. [R. 75.]

4. In a Revenue Agent's report dated August 26, 1930, it was stated that Signal Gasoline Corporation had distributed all its assets to its sole stockholder, Signal Oil and Gas Company, upon its dissolution in December of 1928. [R. 82.]

5. In a letter dated March 30, 1931, from the Commissioner of Internal Revenue, addressed to the Signal Gasoline Corporation, which letter was a 60-day letter proposing additional taxes for the year 1928, it was stated that the Signal Gasoline Corporation had been dissolved in December, 1928. [R. 82-83.]

6. Except for the matters set out above, no other correspondence with the Collector of Internal Revenue was filed by and on behalf of Signal Gasoline Company or Signal Gasoline Corporation after their dissolution and prior to February 16, 1932, excepting as follows:

(a) On January 20, 1932, a letter to the Commissioner was written and signed "Signal Gasoline Corporation, by J. H. Rounsavell, Comptroller" advising the Commissioner to change his records so that all correspondence relative to the income tax matters of Signal Gasoline Corporation for 1924 to 1928 inclusive would be sent to 1200 Signal Oil Building, 811 West Seventh Street, Los Angeles, California. [R. 81.]

(b) On January 20, 1932, a similar letter was written signed "Signal Gasoline Company, by J. H. Rounsavell,

Comptroller" with respect to the Signal Gasoline Company for 1922 to 1924. [R. 81.]

(c) On January 20, 1932, a similar letter was written and signed by Signal Gasoline Company, Inc., by J. H. Rounsavell, Comptroller, with respect to the 1925, 1926, 1927 and 1928 taxes of the Signal Gasoline Company, Inc. [R. 81.]

(d) On July 27, 1931, a letter signed by Signal Gasoline Corporation, by J. H. Rounsavell, Comptroller, was mailed to the Collector at Los Angeles, stating that there was pending before the Board of Tax Appeals the question of whether Signal Gasoline Corporation was liable for the 1923 income tax liability of Signal Gasoline Company. [R. 81-82.]

On February 16, 1932, the Board of Tax Appeals purported to affirm the rulings of the Commissioner of Internal Revenue in asserting the deficiencies appealed from in petitions numbered 41532 and 47620, relating to the income taxes of the Signal Gasoline Company. Said decision of the Board is contained in an opinion reported in 25 B. T. A. 532. [R. 75.]

On September 10, 1932, the Commissioner purported to assess the Signal Gasoline Corporation as a transferee of the Signal Gasoline Company for the above described tax liabilities of Signal Gasoline Company in the amounts and for the taxable periods as follows:

For the taxable year 1923, $468.33 plus interest of $227.96; for the taxable period ended September 11, 1924, $2672.53 plus interest of $1,200.70. [R. 76; Plaintiff's Exhibit J; R. 88-89.]

By reason of the dissolution of the Signal Gasoline Corporation and the disbursement of all its assets to its statutory trustees as above set forth, Signal Gasoline Corporation was and is left without any money, assets or property of any kind, with which to pay said taxes and interest claimed herein by the United States. The assets which were acquired by the appellant, Signal Oil and Gas Company, as sole stockholder of Signal Gasoline Corporation as heretofore shown were far in excess of the taxes and interest prayed for in the complaint herein. [R. 79.]

Due demand for the payment of taxes and interest prayed for in the complaint herein has been made upon the Signal Oil and Gas Company but no portion thereof has been paid. [R. 79.]

At all times herein mentioned and considered, substantially the same persons were officers and directors or statutory trustees of the Signal Gasoline Corporation, as were the officers and directors of the Signal Oil and Gas Company and officers and directors or trustees of the Signal Gasoline Company. [R. 79.]

An offer to compromise the taxes here involved, acknowledged October 31st, 1932, was filed shortly thereafter. It was signed by the Signal Gasoline Corporation, by S. B. Mosher, H. M. Mosher, O. W. March, R. H. Green, and C. Lav. Lazalere. The acknowledgment stated that the above named persons were the statutory trustees of Signal Gasoline Corporation, a dissolved corporation. In the body of the offer it was stated that Signal Gasoline Corporation was dissolved December 12, 1928. [R. 80.]

A similar offer, acknowledged January 23, 1933, and filed shortly thereafter, stated that Signal Gasoline Corporation was dissolved December 12, 1928. It was signed by the Signal Gasoline Corporation, by Melvin D. Wilson, Attorney-in-Fact. In the acknowledgment it was stated that Signal Gasoline Corporation was a dissolved corporation. [R. 80.]

No assessment was ever made against Signal Oil and Gas Company for 1923 and 1924 tax liabilities of the Signal Gasoline Company. No assessment was ever made against the Signal Gasoline Company for the said 1924 tax liability of Signal Gasoline Company. A purported assessment against the Signal Gasoline Company was made July 3, 1931, in the amount of $468.33 plus interest for its said tax liability for the calendar year 1923. [R. 82.]

The appellee brought its suit against appellant on September 9, 1938, at the direction of the Attorney General, with the sanction and at the request of the Commissioner of Internal Revenue. [R. 2, 3.]

This case, Docket No. 1460-Y, was tried before the Honorable Leon R. Yankwich on January 16, 1940, upon a written stipulation of facts and upon documentary evidence being introduced into evidence. [R. 33-41.]

On July 27, 1940, the Judge of the District Court filed his minute order finding for the appellee. [R. 45-46.] The findings of fact and conclusions of law was signed by the District Judge on December 26, 1940, and filed the same day. [R. 48-61.] Judgment in favor of the appellee in the amount of $4,569.52 together with interest at the rate of 12% per annum from September 10th, 1932, to October 24, 1933, and interest at the rate of 6% per annum from October 24, 1933, to date of pay-

ment, together with costs in the sum of $27.14, was signed and entered on the 26th day of December, 1940. [R. 61-63.]

The facts in case No. 1461-Y may be briefly stated as follows:

All the facts stated above with respect to case No. 1460-Y relative to the dissolution of Signal Gasoline Corporation, the distribution of its assets to the statutory trustees, the conveyance by the statutory trustees of the assets to appellant, the various notices given to the Commissioner by the statutory trustees that Signal Gasoline Corporation had been dissolved, the fact that the dissolution of Signal Gasoline Corporation left it unable to pay any tax liabilities, and any other statements made above which are pertinent to this case, are incorporated herein as fully as though herein set forth at this point.

Signal Gasoline Corporation filed its income tax return for the calendar year 1924 on or about May 13, 1925. [R. 76.]

On December 3, 1928, Signal Gasoline Corporation signed and filed Form 852 which is entitled "Consent Fixing Period of Limitation Upon Assessment of Income and Profits Tax"; that document purported to give the Commissioner until December 31, 1929, in which to assess additional income taxes for 1924 against Signal Gasoline Corporation. [Plaintiff's Exhibit 4; R. 91-76.]

On December 12, 1928, the Signal Gasoline Corporation was dissolved as stated heretofore.

On December 28, 1929, the Commissioner of Internal Revenue addressed and mailed a letter to Signal Gasoline Corporation. This letter proposed an assessment of ad-

ditional tax liability against the Signal Gasoline Corporation for the period May 1st to December 31st, 1924, in the amount of $14,137.05. [R. 76.]

On February 24, 1930, a petition was filed with the Board of Tax Appeals for a redetermination of the 1924 deficiency proposed in the Commissioner's letter dated December 28, 1929, above referred to; that said proceeding was therein given Docket No. 47621; that said petition was filed under the name of Signal Gasoline Corporation; that the petition stated in its first paragraph that: "The petitioner is a dissolved California corporation acting through its statutory trustees * * *"; that the verification of the petition was signed by six persons and the verification stated that these six persons were "* * * the statutory trustees of Signal Gasoline Corporation, a dissolved corporation * * *"; the petition was signed by Robert N. Miller and Melvin D. Wilson as attorneys for the petitioner. [R. 77-78.]

Although the Commissioner of Internal Revenue had the various notices given him by the statutory trustees that Signal Gasoline Corporation had been dissolved December in 1928, he made no motion for substitution of the parties during the time the case was pending before the Board of Tax Appeals. [R. 79.]

On March 15, 1932, the Board of Tax Appeals purported to affirm the ruling of the Commissioner of Internal Revenue in asserting the deficiency appealed from in Docket No. 47621. Said decision of the Board is contained in an opinion reported in 25 B. T. A. 861. [R. 78.]

On October 1, 1932, the Commissioner of Internal Revenue purported to assess the Signal Gasoline Corpo-

ration for its tax deficiency for the calendar year 1924 in the principal amount of $14,137.05 plus interest of $6,080.77. [R. 78; Plaintiff's Exhibit 9; R. 97-98.]

Due demand for the payment of the taxes and interest prayed for in this case has been made upon appellant, but no portion thereof has been paid. [R. 79.]

No assessment was ever made against Signal Oil and Gas Company for the tax liability of Signal Gasoline Corporation for the year 1924. [R. 82.]

The appellee brought its suit against appellant on *September 9, 1938,* at the direction of the Attorney General. with the sanction and at the request of the Commissioner of Internal Revenue. [R. 9-16.]

This case, Docket No. 1461-Y, was tried before the Honorable Leon R. Yankwich on January 16, 1940, upon a written stipulation of facts and upon documentary evidence being introduced into evidence. [R. 33-41.]

On July 27, 1940, the Judge of the District Court filed its minute order finding for the appellee. [R. 46-47.] The findings of fact and conclusions of law was signed by the District Judge on December 26, 1940, and filed the same day. [R. 48-61.] Judgment in favor of the appellee in the amount of $20,217.82 together with interest at the rate of 12% per annum from October 1, 1932, to October 24, 1933, and interest at the rate of 6% per annum from October 24, 1933, to the date of payment, and costs in the amount of $27.06.

Specification of Errors Relied Upon.

1. There was no evidence introduced at the trial showing that the taxes sued on were due from anyone. The alleged assessments relied on by the appellee for that purpose were void and prove nothing, having been purportedly made long after the corporation against which they were supposed to have been made had been dissolved and utterly destroyed by its dissolution. Said alleged assessments were based upon alleged proceedings in the Board of Tax Appeals wherein the appellee was guilty of laches in that it did not move for a dismissal or substitution of the petitioner although long having knowledge that the petitioner had been dissolved and destroyed by its dissolution.

2. The suits by appellee were barred by the statute of limitations as they were not brought within four years of the filing of the returns of the corporations whose taxes were involved and no assessment was made against the appellant, but the appellee was relying upon a six-year period within which to sue appellant after alleged assessments against a prior transferee, but the alleged assessments against the prior transferee were invalid for the reason stated in Point 1, and hence do not give a six year period for suit, and even if the assessments against the prior transferee had been valid, they would not give appellee six years within which to sue subsequent transferees.

3. Appellant is not estopped from asserting the bar of the statute of limitations, appellee having at all times been

in possession of all the material facts and having initially made an error of law which error misled the appellant's predecessors into further errors of law, if they made any errors of law, but estoppel does not arise from errors or mutual errors of law.

4. The judgments against appellant should be reversed. [R. 101-103.]

Summary of Argument.

The specification of errors relied upon also constitutes a brief summary of the argument.

ARGUMENT.

1. No Evidence Was Introduced at the Trial Proving That the Taxes Sued Upon Were Due From Anyone. The Alleged Assessments Relied Upon by the Appellee for That Purpose Being Void.

The appellee brought suits in equity against appellant to collect from appellant taxes alleged to be owing from other corporations now dissolved.

Appellee, of course, *has* the burden of proving all the material allegations of its complaints. The appellee, in its complaint, did not even allege that the taxes were due from anyone.

Appellee did allege that assessments had been made against Signal Gasoline Corporation and appellee relied on those assessments as proving that the taxes were due. As will be hereinafter shown, the alleged assessments against Signal Gasoline Corporation were void and raise no presumption that the taxes sought to be recovered herein were due from Signal Gasoline Company, Signal Gasoline Corporation, Signal Oil and Gas Company, or from anyone else.

As shown in the statement of facts, Signal Gasoline Corporation was dissolved in December of 1928. The alleged assessments relied on by the appellee were not made until September 10, 1932, and October 1st, 1932, respectively. [R. 75-78.]

Thus the alleged assessments were made nearly four years after Signal Gasoline Corporation had been dissolved. Said alleged assessments were absolutely void and of no effect whatsoever.

In December of 1928, when Signal Gasoline Corporation was dissolved, Section 400 of the Civil Code of the

State of California read as shown in the appendix to this brief. It will be noted that under such section the last directors ordinarily became the statutory trustees for the creditors and stockholders and had full power to settle any of the affairs of the corporation, collect and pay outstanding debts, sell the assets, and distribute the proceeds to the stockholders. It will be noted that no provision was made for the extension of the corporate existence whatsoever.

Under this provision of the Civil Code, the dissolution of the corporation absolutely destroyed it. In Ballentine on California Corporations, 1931 Edition, P. 476, this proposition is set forth as follows:

> "Corporations dissolved prior to August 14, 1929, are not governed by Section 399, Civil Code, and their corporate existence came to an end under the former Code provision. When a corporation was dissolved, the persons constituting the last Board of Directors became the statutory trustees *ex officio* of the defunct corporation and were charged with the duty of winding up its affairs, even though the technical legal title may have vested in the shareholders. Pending actions against the corporation abated and the directors, as trustees, had to be substituted. As to such corporation, the effect of dissolution was to terminate the legal entity and render the corporation incapable of acting, or of suing, or being sued."

The above quotation is based upon the California Supreme Court cases of *Crossman v. Vivienda Water Company,* 150 Cal. 575, 89 Pac. 335, and *Brandon v. Umqua Lumber Company,* 166 Cal. 322, 136 Pac. 62, 47 A. L. R. 1407. See also 7 *Cal. Jur.* 137-138.

In *7 Cal. Jur.* 138, the following statement appears:

> "A dissolved corporation is incapable of suing or being sued as a corporate body or in its corporate name, there being no one who can appear and act for the corporation, all actions pending against it are abated, and any judgment attempted to be given against it is void—a mere nullity, except as otherwise as provided by statute. Such a void judgment, therefore, is no bar to a subsequent action against the trustees of the corporation."

The above principle of law has been recognized by the United States Circuit Court of Appeals for the Ninth Circuit in *G. M. Standifer Construction Corporation v. Commissioner,* 78 Fed. (2d) 285. In that case an Oregon corporation had dissolved on August 30, 1927, and under the laws of Oregon it continued to exist for five years for the purpose of winding up its affairs. On November 1, 1930, the Commissioner of Internal Revenue sent it a 60-day letter notifying it of a deficiency in its 1928 income tax. On December 29, 1930, the corporation filed with the Board of Tax Appeals a petition for redetermination. On October 2, 1933, after the expiration of the five-year period, the matter was heard by the Board and on June 7, 1934, the Board rendered its decision, to review which a petition was filed in the United States Circuit Court of Appeals for the Ninth Circuit, on October 29, 1934. The Circuit Court, at 78 Fed. (2d), page 286, said:

> "The general effect of the dissolution of a corporation is to put an end to its corporate existence for all purposes whatsoever, and to extinguish its power to sue or be sued, but, if the law of the state of incorporation so provides, its existence may continue for a specified period after dissolution for the pur-

pose of winding up its affairs, and during that extended period of corporate life, it may sue or be sued. Thompson on Corporations, Third Edition, Vol. 8, Secs. 6505, 6530; 14a C. J. 1200, 1201; 7 R. C. L. 735, 743. The rule is stated as follows in Oklahoma Natural Gas Company v. State of Oklahoma, 273 U. S. 257, 259, 47 Sup. Ct. 391, 392, 71 L. Ed. 634:

"'It is well settled that at common law and in the Federal jurisdiction a corporation which has been dissolved is as if it did not exist, and the result of the dissolution cannot be distinguished from the death of a natural person in its effect. (Citing cases.) It follows therefore that, as the death of the natural person abates all pending litigation to which such a person is a party, dissolution of a corporation at common law abates all litigation in which the corporation is appearing either as plaintiff or defendant. To allow actions to continue would be to continue the existence of the corporation *pro hac vice*. But corporations exist for specific purposes and only by legislative act, so that if the life of the corporation is to continue even only for litigating purposes, it is necessary that there should be some statutory authority for the prolongation. The matter is really not procedural or controlled by the rules of the court in which the litigation pends. It concerns the fundamental law of the corporation enacted by the State which brought the corporation into being.'"

This Court, in the *Standifer* case, at page 286, then said:

"Here, the five-year period expired, the corporation became defunct, and the proceeding before the Board of Tax Appeals abated on August 30, 1932, twenty-one months before the Board rendered its decision.

> The petition filed in this court in the name of the defunct corporation presented nothing for review. The only thing we can do with such a petition is to dismiss it."

In that case, the proposed deficiency against the defunct corporation of course became abated and a nullity and it was incumbent upon the Commissioner to proceed against the transferees of the assets of the corporation subject to all the defenses they might raise.

In other tax cases, the principle has also been recognized that a corporation whose legal existence has been completely terminated cannot have a valid assessment, order, or judgment made against it. (*Sanborn Brothers, Successors, etc.,* 14 B. T. A. 1059; *Union Plate and Wire Company,* 17 B. T. A. 1229; *Iberville Wholesale Grocery Company,* 15 B. T. A. 645 and 17 B. T. A. 235; *S. Hirsch Distilling Company,* 14 B. T. A. 1073.)

In the case of *S. Hirsch Distilling Company, supra,* decided January 9, 1929, a Missouri corporation was involved. The statutes of Missouri were like the statutes of California in effect at the time Signal Gasoline Corporation was dissolved. There was no provision for continuing the corporate existence for any purpose, but the last directors were the statutory trustees for the creditors and stockholders. The Board, in discussing the effect of this dissolution of the Missouri corporation, said:

> "In Scanlan v. Crawshaw, 5 Mo. App. 337, it was held that a judgment against the corporation that had ceased to exist at the time it was rendered was a nullity and that an order to issue execution on such judgment against the stockholder was void."

The Board concluded that the S. Hirsch Distilling Company ceased to exist at the time of its dissolution, namely, June 20, 1920, and that all the rights which it, as a corporation, had theretofore had were completely extinguished; that it no longer had any right to do anything and no legal existence or status to institute the proceeding before the Board (in 1926), and the Board's determination of the deficiency under such circumstances would be a nullity, and accordingly, the Board, on its own motion, held that it had no jurisdiction.

As noted above, under California law, a judgment attempted against a corporation dissolved prior to July 14, 1929, is void and a mere nullity. (7 *Cal. Jur.* 138; *California National Supply Company v. Flack,* 183 Cal. 124, 190 Pac. 634; *Hanson v. Choynski,* 180 Cal. 275, 180 Pac. 816; *Llewellyn Iron Works v. Abbott Kinney Co.,* 172 Cal. 210, 155 Pac. 986; *Newhall v. Western Zinc Mining Co.,* 164 Cal. 380, 128 Pac. 1040; *Crossman v. Vivienda Water Company,* 150 Cal. 575, 89 Pac. 335.)

It seems clear therefore that the alleged assessments against Signal Gasoline Corporation in 1932 were an absolute nullity as the corporation had been destroyed by its dissolution in 1928. Consequently, the void assessments do not prove that the alleged tax was due. The taxes involved were never assessed against appellant Signal Oil and Gas Company.

Since there is no evidence that the tax was due from anyone, the appellee cannot collect the said alleged tax from anyone.

2. The Alleged Assessments Being Void Do Not Start a Six-Year Period in Which the Appellee Could Sue Transferees.

The alleged taxes involved in these proceedings related to the years 1923 and 1924 for which returns were filed in 1924 and 1925. The statutory time for bringing suit against the taxpaying corporation or anyone else based on the returns was four years after the returns were filed. (Section 277 (a) (1) of the Revenue Act of 1924.) It is obvious, therefore, that the appellee was not suing the appellant under that section as the suits were not brought until 1938.

No assessment has been made against Signal Oil and Gas Company (for the alleged taxes of its predecessors) and hence the appellee could not have been relying upon Section 278 (d) of the Revenue Act of 1926 which gave the Commissioner six years after an assessment within which to collect tax from the entity assessed.

The appellee was relying upon a six-year period for bringing suit against transferees, under the trust fund theory, based upon alleged assessments against the Signal Gasoline Corporation. (Section 278 (d) of the Revenue Act of 1926.) In other words, the appellee relied upon assessments made in September and October of 1932 and brought the suits just within six years from the date of said purported assessments.

The assessments on which the appellee relied for starting the six-year period for bringing suit were, as shown

above, absolutely void. Consequently, they did not give the Government six years within which to sue anyone. No argument or citation of authority is necessary to support the proposition that legal rights cannot be based upon a nullity.

The alleged assessments on which the appellee was relying to commence the six-year period of limitation for bringing suit being void, the appellee is relegated to the provisions of law which give it four years after the returns for 1923 and 1924 were filed within which to sue alleged transferee. Since the returns were filed in 1924 and 1925, the time for filing suit expired in the spring of 1928 and 1929. The suits having been brought in 1938 are barred by the statute of limitations.

On May 13, 1929, on November 20, 1929, and on February 24, 1930, the Commissioner was advised that Signal Gasoline Corporation had been dissolved. Under Section 280 (b) (1) of the Revenue Act of 1926, appellee had until March 15, 1930, within which to assess the trustees of Signal Gasoline Corporation or the Signal Oil and Gas Company, as the transferee. The appellee's failure to do so was due to its erroneous interpretation of the California law respecting dissolved corporations and not to any fault of the trustees or appellant. The present proceedings are barred by the statute of limitations.

3. If, Contrary to Appellant's Contention, the Alleged Assessments Are Held to Be Valid, They Were Made Against the First Transferees of the Taxpaying Corporations and Said Assessments Did Not Give the Appellee Six Years in Which to Sue Subsequent Transferees.

In Case No. 1460-Y, the facts clearly show that the taxes involved were the 1923 and 1924 taxes of Signal Gasoline Company; that this company dissolved, distributed its assets to Signal Gasoline Corporation; that Signal Gasoline Corporation dissolved and its assets eventually, after passing through its statutory trustees, came over to appellant, Signal Oil and Gas Company.

It is obvious, therefore, that Signal Oil and Gas Company is a transferee of the transferee of the assets of Signal Gasoline Company, the taxpaying corporation.

The Government is relying on a six-year period based upon an assessment made upon the first transferee to sue the second transferee. But the Supreme Court, in *United States v. Continental National Bank and Trust Company,* 305 U. S. 398, very clearly and definitely held that a timely assessment against the first transferee of the assets of the taxpayer did not give the Government six years in which to sue the second transferee of the assets of the taxpayer.

That case is, therefore, squarely in point and directly bars the action in the case of 1460-Y.

The important facts in the two cases are very similar and are as follows:

Description	Continental Case	Case 1460-Y
Taxable years involved:	1920,	1923, 1924
Character of original taxpayer:	Corporation	Corporation
Relation of Appellant to original taxpayer:	Transferee of a Transferee	T. of a T.
Did first transferee file a petition with the Board of Tax Appeals:	Yes	Yes
Was an alleged assessment made against the first transferee? Date	Yes-2-14-31	Yes-9-10-32
Was suit brought against second transferee without assessment against the defendant? Date	Yes-5- 6-32	Yes-9- 9-38
Period between filing of return of original taxpayer and bringing of suit in years	11	13-14
Period between assessment on first transferee and suit against second transferee in years	1¾	6

It is well established, therefore, that even if the assessment against Signal Gasoline Corporation for the taxes alleged to be due from Signal Gasoline Company for the years 1923 and 1924 was valid, that assessment, being on the first transferee, did not give the Government six

years in which to sue the second transferee, namely, appellant.

At the time appellee brought its suit, an assessment against the first transferee was thought to give the Government six years in which to sue subsequent transferees. The appellee doubtless relied on this misapprehension of the law, as it waited five years, eleven months and twenty-nine days before bringing suit. If appellee had not made that mistake of law, it might have taken some other timely action. But appellee did make that mistake of law, and is now casting about, trying to fasten the blame on appellant, by pleading estoppel.

As to the facts in Case No. 1460-Y, therefore, it is clear that the Supreme Court's decision in *U. S. v. Continental Nat. Bk. & Tr. Co.,* is squarely in point, and bars the suit.

In Case No. 1461-Y, the Supreme Court's decision in *U. S. v. Continental Bank and Trust Company* also bars the complaint but the facts do not stand out quite so clearly.

In this case the tax involved was the 1924 tax of Signal Gasoline Corporation. That corporation was dissolved in December of 1928 but the Commissioner of Internal Revenue purported to make an assessment against Signal Gasoline Corporation in October of 1932.

The appellee thought that it had six years from the alleged assessment in October of 1932 against Signal Gasoline Corporation to sue appellant.

Now it is not entirely clear as a matter of law whether the alleged assessment made in October, 1932, was purportedly made against Signal Gasoline Corporation or

against the statutory trustees of Signal Gasoline Corporation.

If the alleged assessment was purportedly made against Signal Gasoline Corporation, then said alleged assessment was void, as Signal Gasoline Corporation had been destroyed in 1928 on its dissolution, and the void assessment would not start a six-year period of limitations within which the Government could sue the transferees and this suit would be barred.

If the appellee contends that the assessment was really against the statutory trustees of the dissolved Signal Gasoline Corporation, then appellant contends that the suit is barred because the statutory trustees were the first transferees of Signal Gasoline Corporation, and an assessment against them as first transferees does not give the Government six years within which to sue appellant who was the second transferee of Signal Gasoline Corporation. (*U. S. v. Continental National Bank and Trust Company*, 305 U. S. 398.)

Appellant suggests that the alleged assessment made in October, 1932, in the name of Signal Gasoline Corporation was really made against the statutory trustees. Section 400 of the Civil Code of California as it stood in 1928 when Signal Gasoline Corporation was dissolved, provided in part as follows:

> "* * * Such trustees shall have authority to sue for and recover the debts and property of the corporation, *and shall be jointly and severally liable to the creditors* and stockholders or members, to the extent of its property and effects that shall come into their hands." (Emphasis supplied.)

It is thus indisputable that the trustees were the first transferees of the assets of Signal Gasoline Corporation.

Section 416 of the Code of Civil Procedure of the State of California as it stood in 1928 and as it stands today, reads in part as follows:

> "In all cases where a corporation has forfeited its charter or right to do business in this state, *the persons who become the trustees of the corporation* and of its stockholders or members *may be sued in the corporate name of such corporation* in like manner as if no forfeiture had occurred and from the time of the service of the summons and a copy of the complaint in a court action, upon one of said trustees, or of the completion of the publication when service by publication is ordered, *the court is deemed to have acquired jurisdiction of all said trustees,* and to have control of all subsequent proceedings * * *" (Emphasis supplied.)

The jurisdiction which the court acquires is not jurisdiction of the dissolved corporation, however, but only of the trustees. (*Crossman v. Vivienda Water Company, supra,* and *7 Cal. Jur.* 176.)

Consequently, the deficiency letter issued on December 28, 1929, in the name of Signal Gasoline Corporation was really issued to the trustees of the dissolved corporation and the petition filed in the name of Signal Gasoline Corporation was really the petition of the trustees. The Board proceedings and assessment were therefore probably valid as to the trustees but not as to the corporation.

The Government had six years from October 1, 1932, to sue the trustees, but did not do so. The suit against

the appellant herein, the second transferee, was not brought within four years of the filing of the return and is barred by the statute of limitations, the assessment against the trustees (the first transferees) not giving the Government six years within which to sue subsequent transferees. *(U. S. v. Continental Bank and Trust Company, supra.)*

In *Buzzard v. Helvering,* 77 Fed. (2d) 391, the statutory trustees of a dissolved California corporation filed an appeal with the Board of Tax Appeals, as trustees, but the petition was filed in the name of the dissolved company. The Court, after citing Section 400 of the Civil Code of California and *Crossman v. Vivienda Water Company, supra,* at page 395, said:

> "* * * The appeal from the deficiency notice, we think, was an appeal by the trustees of the lumber company, however it may have been styled in the hearings or in the pleadings."

Again at page 395 the court said:

> "* * * and we think it also clear that the decision of the Board, sustaining the deficiency notice of the Commissioner, was no more or less than an ascertainment of the validity of the debt of the lumber company for which, under the tax statutes, petitioners, as trustees, were liable and bound to account under the tax laws and under the California statute."

Also on the same page the court said:

> "In this view we hold (1) * * *; (2) that the petition filed April 11, 1925, by the trustees for a redetermination of the deficiencies, however styled, was in legal effect an appeal by the trustees appointed to administer the affairs of the dissolved corporation; * * *"

Similarly in the case at bar the appeal filed by the statutory trustees of Signal Gasoline Corporation, though styled in the name of the corporation, was really an appeal by the trustees.

Since the appeal was filed by the trustees, the subsequent assessment was also against the trustees.

But as shown by the decision of the Supreme Court of the United States in *U. S. v. Continental Bank and Trust Company, supra,* an assessment made against the statutory trustees as first transferees does not give the Government six years within which to sue the second or later transferees, namely, the appellant herein.

It is apparent, therefore, that the deficiency letter issued by the Commissioner of Internal Revenue addressed to Signal Gasoline Corporation after that corporation has been dissolved and under California law utterly destroyed, was really addressed to the statutory trustees as transferees, and the petition they filed was in the capacity as trustees and transferees.

Under that view of the case, the proceeding before the Board and the assessment were valid as to the trustees, but since this was an assessment against the first transferees of the taxpayer corporation, Signal Gasoline Corporation, that assessment did not give the Government six years within which to sue the second transferee, namely, Signal Oil and Gas Company. *(U. S. v. Continental Bank and Trust Company, supra.)*

Summarizing as to Case No. 1461-Y, it seems clear from the law and the facts that if the purported proceeding before the Board and the purported assessment related to Signal Gasoline Corporation, they were entirely null

and void and there is no evidence that any additional tax is due, as that corporation had been dissolved long before the purported assessment was made. Consequently, the appellee cannot base a six year period to sue appellant upon such void assessment.

On the other hand, if the proceedings before the Board and the assessment related to the statutory trustees of Signal Gasoline Corporation, a dissolved corporation, then such assessment was probably valid and is evidence that the additional tax is owing but such assessment was against the first transferees of Signal Gasoline Corporation and this assessment does not give the Government six years within which to sue the subsequent transferee, namely, appellant.

Consequently, the complaint in Case No. 1461-Y is barred by the statute of limitations.

4. Statute of Limitations Provisions in Taxing Statutes Must Be Strictly Construed Against the Government.

In *United States v. Updike,* 281 U. S. 489, the Supreme Court of the United States, p. 496, said:

> "In any event, we think this is a fair interpretation of the clause, and the one which must be accepted, especially in view of the rule which requires taxing acts, including provisions of limitations embodied therein, to be construed strictly in favor of the taxpayer. Bowers v. New York & Albany Company, 273 U. S. 346, 349, 47 Supr. Ct. 389, 71 Law Ed. 676."

In *Bowers v. New York & Albany Lighterage Company, supra,* the court, among other things, said at page 390:

> "The provision (limitation) is a part of the taxing statute; and such laws are to be interpreted liberally in favor of the taxpayers. Eidman v. Martinez, 184 U. S. 578, 583, 22 S. Ct. 515, 46 Law. Ed. 697; Shwab v. Doyle, 258 U. S. 529, 536, 42 S. Ct. 391, 66 Law. Ed. 746, 26 A. L. R. 1454."

If there is any doubt about the statute of limitations point in this case, the doubt must be resolved in favor of the taxpayer and not in favor of the Government. There is nothing inequitable in pleading the statute of limitations; certainly nothing inequitable in pleading the statute of limitations when the appellee brings suit in 1938 on a presumed assessment made in 1932 for the 1923 and 1924 taxes of other corporations whose assets passed through the hands of three successive transferees before reaching the appellant.

As said by the Supreme Court in *United States v. Updike,* 281 U. S. 489, 495:

> "In such case, to allow an indefinite time for proceeding to collect the tax would be out of harmony with the obvious policy of the act to promote repose by fixing a definite period after assessment within which suits and proceedings for the collection of taxes must be brought."

5. **Appellant Is Not Estopped From Asserting the Bar of the Statute of Limitations, Appellee Having at All Times Been in Possession of All the Material Facts and Having Initially Made an Error of Law Which Error Misled the Appellant's Predecessors Into Further Errors of Law, if They Made Any Errors of Law, But Estoppel Does Not Arise From Errors or Mutual Errors of Law.**

In the conclusions of law approved by the District Court [Tr. p. 60] the following is included:

> "That the defendant is estopped from setting up the bar of the statute of limitations to the causes of action set forth in complaints No. 1460-Y and 1461-Y."

Apparently the acts relied upon by the appellee to establish the estoppel are as follows:

1. A series of corporations each having in its name the word "Signal" have been in existence and have dissolved, distributing their assets to their successors, the assets finally reaching the appellant. But appellee never had any difficulty in determining the separate tax liabilities of the several corporate entities.

2. On May 13, 1929, the corporation income tax return for 1928 was filed with the Collector of Internal Revenue at Los Angeles, California, on behalf of the Signal Gasoline Corporation and was signed by S. B. Mosher, as president, and O. W. March, as treasurer, of the said corporation. But the return stated that Signal Gasoline Corporation had been dissolved in December of 1928.

3. Petitions in the name of Signal Gasoline Corporation were filed with the Board of Tax Appeals on February 24, 1930, after Signal Gasoline Corporation had been

dissolved. But these petitions stated that Signal Gasoline Corporation had been dissolved and that the statutory trustees were acting.

4. A protest against a proposed deficiency for 1927 income tax of Signal Gasoline Corporation was signed about November 20, 1929. This protest was signed "Signal Gasoline Corporation, by S. B. Mosher". But at the left of said signature five other trustees of the dissolved corporation signed their names. The protest was verified by Melvin D. Wilson, one of the attorneys in fact and in law, which stated that he had verified it for the reason that when the statutory trustees signed the protest, they neglected to acknowledge it before a notary public.

5. On July 27, 1931, a letter signed "Signal Gasoline Corporation, by J. H. Rounsavell, Comptroller", was mailed to the Collector at Los Angeles, California, stating that there was pending before the United States Board of Tax Appeals the question of whether Signal Gasoline Corporation was liable for the 1923 income tax liability of Signal Gasoline Company. But this letter, and the letters mentioned in the following three paragraphs, were not written until more than two years after the Commissioner had been informed of the dissolution of Signal Gasoline Corporation. Furthermore, J. H. Rounsavell was not the statutory trustee of the dissolved corporation; nor even one of them. Consequently, he had no standing or authority to represent the dissolved corporation, or the trustees.

6. On January 20, 1932, a letter to the Commissioner of Internal Revenue was written and signed "Signal Gasoline Corporation, by J. H. Rounsavell, Comptroller", advising the Commissioner to change his records so that all

correspondence relative to the income tax matters of the Signal Gasoline Corporation for 1924 and 1928 inclusive would be sent to 1200 Signal Oil Building, 811 West Seventh Street, Los Angeles, California. [Tr. p. 81.]

7. On January 20, 1932, a letter to the Commissioner signed "Signal Gasoline Company, by J. H. Rounsavell, Comptroller", was mailed advising the Commissioner to change his records so that all correspondence pertaining to the income tax liability of Signal Gasoline Company for 1922 to 1924, inclusive, would be sent to 1200 Signal Oil Building, 811 West Seventh Street, Los Angeles, California.

8. On January 20, 1932, a letter to the Commissioner signed "Signal Gasoline Company, Inc., by J. H. Rounsavell, Comptroller", was mailed advising the Commissioner to change his records so that all correspondence pertaining to the income tax liability of Signal Gasoline Company, Inc. for 1925, 1926, 1927, and 1928, inclusive, would be sent to 1200 Signal Oil Building, 811 West Seventh Street, Los Angeles, California.

9. An offer to compromise the taxes here involved, acknowledged October 21, 1932, was filed shortly thereafter. It was signed "Signal Gasoline Corporation, by S. B. Mosher, H. M. Mosher, O. W. March, R. H. Green. C. Lav. Lazalere". In the body of the compromise and in the acknowledgment it was stated that the corporation had been dissolved and that the persons who signed the protest were the statutory trustees of the dissolved corporation.

10. A similar offer, acknowledged January 23, 1933, and filed shortly thereafter, stated that Signal Gasoline Corporation was dissolved December 12, 1928. It was

signed "Signal Gasoline Corporation, by Melvin D. Wilson, Attorney in Fact". The acknowledgment as well as the offer itself stated that Signal Gasoline Corporation was a dissolved corporation.

11. That at all times herein mentioned and considered, substantially the same persons were officers and directors or statutory trustees of the Signal Gasoline Corporation, as were the officers and directors of the Signal Oil and Gas Company and officers and directors or trustees of Signal Gasoline Company. [Tr. p. 57, par. 22.]

12. That in addition to the acts heretofore described, the statutory trustees of the Signal Gasoline Corporation after its dissolution, who were those persons who were the officers and directors of the defendant, persisted in transacting business affairs of the dissolved corporation in the name of the Signal Gasoline Corporation, and in particular the negotiations with the United States of America regarding the tax liabilities of the Signal Gasoline Corporation. [Tr. p. 58, par. 25.]

13. The attorneys who represented the former corporations before the Board and before the Bureau of Internal Revenue are now representing the appellant in the case at bar.

The appellee argued for estoppel in the court below and induced the court to include the doctrine of estoppel in the court's conclusions of law.

It is difficult to understand the District Court's minute order in Case No. 1460-Y [Tr. pp. 45-46] unless it is assumed that the court relied on the doctrine of estoppel. The court said that the assessment against Signal Gasoline Corporation was valid. It then said that the case

was not the case of a suit against the transferee of a transferee and hence the taxpayer could not invoke the doctrine of *United States v. Continental National Bank and Trust Company.*

It was perfectly clear before the District Court as it is here that Signal Gasoline Corporation was the transferee of the assets of the Signal Gasoline Company and that appellant is the tranferee of the assets of the Signal Gasoline Corporation. Since the tax involved in Case No. 1460-Y relates to the 1923 and 1924 taxes of Signal Gasoline Company, it is too clear for argument that the case involved here is a suit against the transferee of a transferee.

If we assume that the District Court understood the facts, then we must assume that the District Court in effect held that this entire chain of corporations constituted one corporation by the doctrine of estoppel, and that the assessment against the Signal Gasoline Corporation for the tax of the Signal Gasoline Company was in effect an assessment against the appellant.

In Case No. 1461-Y, the District Court apparently did not rely on the doctrine of estoppel, but simply relied on the case of *McPherson v. Commissioner,* 54 Fed. (2d) 751, to the effect that the assessment against Signal Gasoline Corporation was valid as against that corporation and was not an assessment against the statutory trustees.

In other words, in Case No. 1460-Y the court seems to have relied on the doctrine of estoppel, whereas in the Case No. 1461-Y it did not rely on that doctrine but apparently relied on the case of *McPherson v. Commissioner, supra.*

(a) The Estoppel Point.

The elements of estoppel are too well known to this court to require extensive citation of authority. In *Van Antwerp v. U. S.*, 92 Fed. (2d) 871, statements relative to estoppel were made at page 875 as follows:

> "The burden of proving every essential element of an estoppel is upon the parties seeking to set up an estoppel. Hanneman v. Richter, 177 Fed. (2d) 563, 566; Merrill v. Tobin, 30 Fed. 738, 743; Mackey Wall Plaster Company v. U. S. Gypsum Company, 244 Fed. 275, 277; Hull v. Commissioner, 87 Fed. (2d) 260, 262; Commissioner v. Union Pacific Railroad Company, 86 Fed. (2d) 637, 640.
>
> "These essential elements of estoppel, each of which the Government must prove in this case, are set up in an authority cited in the Government's brief;
>
> "To constitute estoppel (1) there must be false representation or wrongful misleading silence. (2) The error must originate in a statement of fact and not in an opinion or a statement of law. (3) The person claiming the benefits of estoppel must be ignorant of the true facts, and (4) be adversely affected by the acts or statements of the person against whom an estoppel is claimed.
>
> "U. S. v. Scott & Son, C. C. A. 1, 69 Fed. (2d) 728, 732."

See, also, to the same effect, *Helvering v. Brooklyn City Railroad Company,* 72 Fed. (2d) 274; *Tidewater Oil Company,* 29 B. T. A. 1208; *Merten's Law of Federal Income Taxation,* 1939, Cum. Suppl. 2511-12-13.

The evidence shows very clearly that the Commissioner of Internal Revenue treated all the corporations involved

as separate corporations, computed their income and their tax liabilities separately, issued separate deficiency letters, and throughout clearly recognized the separate corporate entities.

The evidence shows that the Commissioner was notified of the dissolution of Signal Gasoline Corporation as follows :

On May 13, 1929 [R. 82, par. aa];

November 20, 1929 [R. 79-80-95-6-7; Plaintiff's Ex. 7];

February 24, 1930 [R. 75].

The Commissioner indicated that he knew of the dissolution in 1928, of Signal Gasoline Corporation as early as August 16, 1930, and March 30, 1931, as his communications so stated. [R. 82-3.]

Thus the Commissioner knew within six months after the dissolution of Signal Gasoline Corporation that it had been dissolved. The Commissioner knew this for approximately twenty months before the Board of Tax Appeals purported to render its decision against Signal Gasoline Corporation.

Consequently there was no misrepresentation or concealment of material facts by Signal Gasoline Corporation to the Commissioner of Internal Revenue. The facts were as well known to the Commissioner as they were to the trustees of the former corporation. There was no intention on the part of the trustees of the dissolved Signal Gasoline Corporation that the Commissioner, the Board of Tax Appeals, or anyone else should treat Signal Gasoline Corporation as though it were still in existence. The

trustees notified everyone with whom they came in contact that Signal Gasoline Corporation had been dissolved.

The Commissioner did not rely upon the supposed continued existence of Signal Gasoline Corporation. The Commissioner knew long before he proceeded against Signal Gasoline Corporation for the 1923-1924 taxes that the latter had been dissolved. He knew in May of 1929 that the Signal Gasoline Corporation had been dissolved whereas he did not proceed against it for the 1924 taxes until December of 1929.

When, in the petition filed February 24, 1930, the Commissioner was again notified that Signal Gasoline Corporation had been dissolved, he had until December 31st, 1930, to assess the trustees or the appellant herein. (Sec. 280 (b) (1) Revenue Act of 1926.) That he did not do so was due to no fault of the trustees or the appellant.

As a matter of fact, the Commissioner simply made a mistake of law as to the effect of Section 400 of the Civil Code of California. The Commissioner was presumed to know the law of California and therefore was presumed to know that Signal Gasoline Corporation had been completely destroyed upon its dissolution in December of 1928. In fact, the Commissioner had knowledge that under California laws a corporation was completely destroyed by its dissolution. See *Sanborn Bros. Successors,* 14 B. T. A. 1059, decided Jan. 8, 1929. In that case the headnote of the Board's decision reads as follows:

> "A corporation of California had forfeited its charter in 1917 under the California statute of 1915, and under California law its affairs thereafter were in the hands of the former directors as trustees. Respondent determined deficiencies against the corpora-

tion for 1919 and the former stockholders, by one of their number, filed a petition with the Board. Held, since the stockholders are not the persons against whom the deficiency has been determined and has no authority to represent such persons, the Board has no jurisdiction."

Inasmuch as the Commissioner at the time he issued his deficiency notice on December 28, 1929, had been informed that Signal Gasoline Corporation had been dissolved, the Commissioner's action in addressing the dissolved corporation as Signal Gasoline Corporation really led the trustees of Signal Gasoline Corporation to file an appeal with the United States Board of Tax Appeals in the name of Signal Gasoline Corporation. The petition stated, however, that the corporation had been dissolved and the dissolved corporation was acting through its statutory trustees.

If the petition was not properly entitled in order to constitute a pleading by the trustees as such, the error was one of law and was induced by the manner in which the Commissioner addressed the deficiency letter.

It is well established that estoppel cannot exist as to a mistake or mutual mistake of law, or as to an expression of opinion, as distinguished from a representation of facts. (*Helvering v. Salvage,* 297 U. S. 106; *Van Antwerp v. U. S.,* 92 Fed. (2d) 871; *Hawke v. Commissioner,* 109 Fed. (2d) 946; *Tidewater Oil Co.,* 29 B. T. A. 1208; *S. F. Scott & Son v. Commissioner,* 69 Fed. (2d) 728; *Union Pacific R. R. Co.,* 32 B. T. A. 383, affirmed in *Commissioner v. Union Pacific R. R. Co.,* 86 Fed. (2d) 637; *U. S. v. Dickinson,* 95 Fed. (2d) 65; *Grand Central Public Market, Inc. v. U. S.,* 22 Fed. Supp. 119, appeal dismissed 98 Fed. (2d) 1023, C. C. A. 9.)

The Commissioner had a large number of skilled employees, attorneys and others engaged in collecting taxes in California, and certainly had as much opportunity to know the law of California as did the trustees of the dissolved corporation. The Commissioner deals with hundreds of cases of corporations and dissolved corporations, whereas the trustees had only the one case. When the Commissioner wrote to the dissolved corporation in the name of the former corporation, he led the trustees and their counsel into thinking that that was the proper manner in which the trustees of a dissolved corporation would handle its tax matters.

It is very doubtful if any mistake of law has been made by appellant's predecessors or their trustees.

As a matter of law, the deficiency letters issued in the name of Signal Gasoline Corporation, after it had been dissolved, was probably a letter issued to the trustees, and the petition filed by the trustees in the name of the dissolved corporation was a petition by and for the trustees. (See the discussion on this point, pp. 26 to 31, incl.)

But an assessment against the trustees (first transferees) would not give the Government six years to sue the appellant, who was a subsequent transferee (second transferee). *(U. S. v. Continental National Bank & Trust Co., supra.)* Probably the only mistake which has been made, was the appellee's erroneous opinion that a valid assessment against the first transferee would give it six years to sue the second transferee.

Furthermore, the acts upon which appellee would base its estoppel are not the acts of the appellant, but of corporations whose existence has long since been terminated by law, or the trustees thereof.

Appellant should not be estopped from pleading the statute of limitations.

(b) The McPherson Case.

In its minute order in Case No. 1461-Y, the court below relied on the case of *McPherson v. Commissioner*, 54 Fed. (2d) 751, as its authority for the proposition that the purported assessments against Signal Gasoline Corporation were valid, even though that corporation had long before been dissolved.

The *McPherson* case was decided by this court, and related to a dissolved California corporation. The lower court apparently felt bound by that decision, even though, in *G. M. Standifer Construction Corporation v. Commissioner*, 78 Fed. (2d) 285, this court more thoroughly considered the law as to the effect of the dissolution of a corporation, when no provision is made for continuing the corporate existence. In the latter case, this court held that a dissolution under laws similar to California's applicable law completely destroys the corporation and no subsequent proceedings affecting it are valid.

It is very apparent that, in the *McPherson* case, there was not called to the attention of the court the California cases holding that corporations dissolved before July 14, 1929, were absolutely destroyed, whereas corporations dissolved thereafter continue to exist for the purpose of winding up their affairs.

Furthermore, in the *McPherson* case, the statutory trustees signed a waiver of the statute of limitations, designating themselves as surviving trustees of Leighton's, Inc., a dissolved corporation taxpayer. It will be noted that the waiver was by the trustees and not by the cor-

poration and that the trustees did not appeal a later deficiency notice and consequently an assessment was made in the name of the corporation, but apparently against the statutory trustees, as a matter of law. Within the statutory time thereafter, the Commissioner proceeded against the trustees individually, as transferees of the assets of the former corporation.

The court, in the *McPherson* case, said that whether the former corporation was designated by its name or under the term "a dissolved corporation", or as "a dissolved corporation in the hands of trustees", served to suggest a matter of form only and not one attended by substantial differences. That was possibly true in the *McPherson* case since the statutory trustees had given a waiver as trustees, and it is reasonable to suppose that the further proceedings by the Commissioner were against the statutory trustees.

In Case No. 1461-Y, however, it makes a difference whether the alleged assessment was against Signal Gasoline Corporation, or against the statutory trustees. If against the corporation, and if, contrary to appellant's contentions, it were held valid, it would possibly give appellee six years within which to sue first or even second transferees of the assets.

On the other hand, if the assessment was against the statutory trustees, it would be valid. But since the statutory trustees were the first transferees of the assets of Signal Gasoline Corporation, a valid assessment against

them would not give the appellee six years in which to sue the second transferee, namely, appellant. *(U. S. v. Continental National Bank & Trust Co., supra.)*

It should be noted that the decision of this court in *McPherson v. Commissioner,* supra, is not based upon the grounds of estoppel; consequently, it must be considered that the decision was overruled by this court in its later decision in the case of *G. M. Standifer Construction Company v. Commissioner,* 78 Fed. (2d) 285; or if not so overruled, then it is submitted that the *McPherson* case is not, since the decision of the Supreme Court in *U. S. v. Continental National Bank & Trust Co., supra,* good law, since to ignore the difference between making a void assessment against a dissolved corporation or a valid assessment against its statutory trustees, does not give the principle announced in the *U. S. v. Continental* case a chance to operate.

In any event, in the *McPherson* case, the suit before this court (and probably the assessment itself) was against the first transferees, namely, the statutory trustees, whereas in the cases at bar, the suits are against the second transferees. Since the *McPherson* case was decided, the Supreme Court has held that an assessment against the first transferees does not give the Government six years in which to sue second transferees.

Consequently, the *McPherson* case does not establish the solidity of the assessment against Signal Gasoline Corporation.

Summary.

It is respectfully submitted that the suits herein are barred by the statute of limitations because brought more than four years after the taxpayer corporations filed their 1923 and 1924 income tax returns; because the Commissioner of Internal Revenue never assessed the alleged tax against the appellant herein; because the alleged assessments against Signal Gasoline Corporation were invalid and hence there is no evidence that any tax is owing from anyone, and do not create a basis for a six year period for suit; and even if there had been a valid assessment against that corporation or its trustees, this would not have given the appellee six years within which to sue appellant, second transferee of the assets of the taxpayer corporation; that the Supreme Court decision in *U. S. v. Continental National Bank & Trust Co., supra,* is squarely in point; that neither appellant nor any of the predecessor companies nor trustees of dissolved corporations have concealed from, or misrepresented any facts to, the Commissioner of Internal Revenue; and if any mistake was made, it was originated by the Commissioner, who made a mistake of law, and if any of the taxpayers made a mistake, it was a mistake of law induced by the mistake of the Commissioner, but no estoppel is based upon innocent or mutual mistakes of law.

The judgments against appellant should be reversed.

Respectfully submitted,

MELVIN D. WILSON,
Attorney for Appellant.

APPENDIX.

Statutes Involved.

Section 277(a)(1) of the Revenue Act of 1924 provides as follows:

"The amount of income, excess profits, and war-profits taxes imposed by the Revenue Act of 1921, and by such Act as amended, for the taxable year 1921, and succeeding taxable years, and the amount of income taxes imposed by this Act, shall be assessed within four years after the return was filed, and no proceeding in court for the collection of such taxes shall be begun after the expiration of such period."

Section 278(d) of the Revenue Act of 1926 reads as follows:

"Where the assessment of any income, excess-profits, or war-profits tax imposed by this Title or by prior Acts of Congress has been made (whether before or after the enactment of this Act) within the statutory period of limitation properly applicable thereto, such tax may be collected by distraint, or by a proceeding in court (begun before or after the enactment of this Act), but only if begun (1) within six years after the assessment of the tax, or (2) prior to the expiration of any period for collection agreed upon in writing by the Commissioner and the taxpayer."

Section 400 of the Civil Code of California, in effect until August 14, 1929, provided as follows:

"Sec. 400. DIRECTORS, TRUSTEES OF CREDITORS, ON DISSOLUTION. Unless other persons are appointed by the court, the directors or managers of the affairs of a corporation at the time of its dissolution are trustees of the

creditors and stockholders or members of the corporation dissolved, and have full powers to settle the affairs of the corporation, collect and pay outstanding debts, sell the assets thereof in such manner as the court shall direct, and distribute the proceeds of such sales and all other assets to the stockholders. Such trustees shall have authority to sue for and recover the debts and property of the corporation, and shall be jointly and severally personally liable to its creditors and stockholders or members, to the extent of its property and effects that shall come into their hands. Death, resignation or failure or inability to act shall constitute a vacancy in the position of trustee, which vacancy shall be filled by appointment by the Superior Court upon petition of any person or creditor interested in the property of such corporation. Such trustees may be sued in any court in this state by any person having a claim against such corporation or its property. Trustees of corporations heretofore dissolved or whose charters have heretofore been forfeited by law shall have and discharge in the same manner and under the same obligations, all the powers and duties herein prescribed. Vacancies in the office of trustees of such corporation shall be filled as hereinbefore provided; provided, however, that any deed executed in the name of such corporation by the president or vice-president and secretary or assistant secretary after a dissolution thereof or after a forfeiture of the charter of such corporation or after the suspension of the corporate rights, privileges and powers of such corporation, which deed shall have been duly recorded in the proper book of records of the county in which the land or any portion thereof so conveyed is situated, for a period of five years, shall have the same force and effect as if executed and delivered prior to said dissolution, forfeiture or suspension."

No. 9813.

IN THE

United States Circuit Court of Appeals

FOR THE NINTH CIRCUIT

SIGNAL OIL AND GAS COMPANY, a corporation,

Appellant,

vs.

UNITED STATES,

Appellee.

Upon Appeal from the District Court of the United States for the Southern District of California, Southern Division.

BRIEF FOR THE UNITED STATES.

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No. 9813.

IN THE

United States Circuit Court of Appeals

FOR THE NINTH CIRCUIT

SIGNAL OIL AND GAS COMPANY, a corporation,

Appellant,

vs.

UNITED STATES,

Appellee.

BRIEF FOR THE UNITED STATES.

Opinion Below.

The opinions of the District Court [R. 45-47] are not reported.

Jurisdiction.

This is a consolidated appeal from judgments entered for the United States in the amounts of $20,217.82 and $4,569.52 with interest as provided by law on December 26, 1940. [R. 61-63.] Notices of appeal were filed on March 20, 1941. [R. 63-65.] The jurisdiction of this Court is invoked under Section 128(a) of the Judicial Code as amended by the Act of February 13, 1925.

Questions Presented.

1. Whether certain assessments against the Signal Gasoline Corporation are invalid and subject to attack in these suits against the transferee of the Signal Gasoline Corporation to collect such assessments.

2. Whether these suits are barred by the statute of limitations.

Statutes Involved.

The applicable statutes will be found in the Appendix, *infra,* pages 1 *et seq.*

Statement.

A. Preliminary Statement.

The basic facts indicating the nature of these suits which have been consolidated on this appeal may be briefly stated. Corporation A (Signal Gasoline Company) transferred its assets and liabilities to Corporation B (Signal Gasoline Corporation) in return for B's stock. Corporation A was dissolved and the stock distributed to its shareholders. Corporation C (the appellant Signal Oil and Gas Company) acquired all the stock of B which it liquidated, taking over all of B's assets. Two suits were brought by the United States against C to recover:

(1) Income taxes assessed against B for 1923 and 1924 as the transferee of A. (Case No. 1460-Y.)

(2) Income taxes assessed against B for 1924 as the original taxpayer. (Case No. 1461-Y, formerly 1461-RJ.)

B. Details of Corporate Changes and Activities.

On May 1, 1924, pursuant to an agreement between the Signal Gasoline Company, a California corporation, and the Signal Gasoline Corporation, a California corporation, all the assets of the Signal Gasoline Company were turned over to the Signal Gasoline Corporation for 400,000 shares of stock of the Signal Gasoline Corporation, and on September 11, 1924, the Signal Gasoline Company was dissolved; the 400,000 shares received by the Signal Gasoline Company in exchange for its assets and liabilities were distributed to its stockholders. [R. 49-50.]

The Signal Gasoline Company, Incorporated, a corporation now dissolved, was prior to its dissolution a holding company for the stock of the Signal Gasoline Corporation. On July 31, 1928, it owned 419,500 shares of the stock of the Signal Gasoline Corporation, which was 93.22% of the outstanding 450,005 shares of the Signal Gasoline Corporation; the balance of 30,505 shares of the stock outstanding of the Signal Gasoline Corporation (6.78%)[1] was owned by individual stockholders of the Signal Gasoline Company, Incorporated. [R. 50.]

On August 1, 1928, the appellant, Signal Oil and Gas Company, acquired all the assets of the Signal Gasoline Company, Incorporated, which, as noted above, included 93.22% of the stock of the Signal Gasoline Corporation. In November, 1928, the appellant acquired the remaining

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[1]Throughout the record this is referred to as 4.23%; obviously, a mathematical error.

6.78% of the outstanding stock of the Signal Gasoline Corporation from the individual stockholders of the Signal Gasoline Company. [R. 50-51.]

The Signal Gasoline Corporation was dissolved by court decree on December 12, 1928. This decree of dissolution reads in part as follows [R. 86, 87-88]:

> The voluntary application for dissolution of the Signal Gasoline Corporation, a domestic corporation, coming on regularly this day for hearing and determination, the Court finds: * * * 5. * * * that the Board of Directors of said corporation under its Articles of Incorporation consisted of six (6) members and does now consist of six (6) members, namely:
>
> S. B. Mosher
> O. W. March
> Ross McCollum
> H. M. Mosher
> C. LaV. Larzelere
> R. H. Green.
>
> Wherefore, it is Ordered, Adjudged and Decreed, that said Corporation, the Signal Gasoline Corporation be, and the same is, and is hereby declared to be dissolved. It is further Ordered and Decreed that said S. B. Mosher, H. M. Mosher, O. W. March, Ross McCollum, C. LaV. Larzelere and R. H. Green are entitled to be, and are by the Court herein appointed, trustees for the stockholders of said corporation, with power and direction to settle all the affairs of said corporation, and to distribute and convey all the property of said corporation to each of said stockholders, in proportion to the number of shares owned and held by said stockholders when said distribution and conveyance shall be made. * * *

On December 14, 1928, all of the assets of the Signal Gasoline Corporation were conveyed to the appellant subject to all liabilities, including taxes, of the Signal Gasoline Corporation. [R. 51.] This conveyance reads in part as follows [R. 83, 84]:

> That whereas, on the 12th day of December, 1928, the Superior Court of the State of California in and for the County of Los Angeles made and filed its decree dissolving the Signal Gasoline Corporation, * * * Now therefore, in consideration of the premises S. B. Mosher, H. M. Mosher, O. W. March, Ross McCollum, C. LaV. Larzelere and E. H. Green, as Trustees for the stockholders of said Signal Gasoline Corporation, a dissolved corporation, and also in their individual capacities, do hereby assign, transfer, grant, convey, deliver and distribute to said Signal Oil and Gas Company, a Delaware corporation, all of the assets, business and property * * * possessed by said dissolved corporation at the time of its dissolution, * * * and subject to all outstanding obligations and liabilities thereon, and subject to the payment of income taxes that may be due to the United States Government covering operations of said dissolved corporation during the current year and all sums that may be found due covering income taxes for previous years. * * *

By reason of this dissolution and distribution the Signal Gasoline Corporation was and is left without any money, assets or property to pay the taxes hereinafter shown to be due the United States. [R. 56.] The assets so acquired by the appellant were far in excess of such taxes. [R. 57.]

At all times involved substantially the same persons were officers and directors or statutory trustees of the Signal Gasoline Corporation as were the officers and directors of the appellant, and officers and directors of the Signal Gasoline Company, Incorporated. [R. 57.]

In addition to the acts subsequently described, the statutory trustees of the Signal Gasoline Corporation after its dissolution, who were those persons who were the officers and directors of the appellant, persisted in transacting business affairs of the dissolved corporation in the name of the Signal Gasoline Corporation and in particular in the negotiations with the United States of America regarding the tax liabilities of the Signal Gasoline Corporation. [R. 58.]

C. Facts Concerning Assessments Against Signal Gasoline Corporation.

The details concerning the assessments against the Signal Gasoline Corporation are given under Argument I. The following general facts may here be noted.

In October, 1928, the Commissioner of Internal Revenue proposed a tax deficiency against the Signal Gasoline Corporation for the year 1923 as transferee of the Signal Gasoline Company. [R. 5-6.] In December, 1929, a similar tax deficiency was proposed for the year 1924. [R. 6.] The Signal Gasoline Corporation through its trustees prosecuted petitions for redetermination of these taxes by the Board of Tax Appeals. The Board sustained the Commissioner's determinations, 25 B. T. A. 532, and assessments were accordingly made on Septem-

ber 10, 1932. [R. 52-53.] Suit was instituted on September 9, 1938, against these appellants to collect the assessments. [R. 2-9.]

In September, 1929, the Commissioner of Internal Revenue proposed a tax deficiency against the Signal Gasoline Corporation as an original taxpayer for the year 1924. Through its trustees it prosecuted a petition for redetermination of the taxes by the Board of Tax Appeals. The Board sustained the Commissioner's determination, 25 B. T. A. 861, and an assessment was accordingly made on October 1, 1932. [R. 54-56.] Suit was instituted on September 9, 1938, against these appellants to collect the assessment. [R. 9-15.]

The District Court entered judgment for the United States in both cases [R. 61-63] and these consolidated appeals were thereafter taken. [R. 63-65.]

Summary of Argument.

The assessments against the Signal Oil Corporation are valid. They were entered pursuant to decisions of the Board of Tax Appeals in proceedings instituted and prosecuted by the corporation through its duly authorized trustees.

The statute of limitations does not bar these suits. Tax assessments may be collected by proceedings in court commenced within six years after the assessments were made. The assessments against the Signal Gasoline Corporation were entered on September 10, 1932, and October 1, 1932. These suits were instituted on September 9, 1938.

ARGUMENT.

I.

The Assessments Against the Signal Gasoline Corporation Were Valid and May Not Be Questioned by the Appellant.

These suits are based upon three assessments made in 1932 against the Signal Gasoline Corporation, the corporation whose assets were received by the appellant. The validity of the assessments is questioned by the appellant. The facts concerning them are as follows:

A. Assessments Against Signal Gasoline Corporation as Transferee of Signal Gasoline Company.

On October 2, 1928, the Commissioner of Internal Revenue mailed a letter to the Signal Gasoline Corporation proposing a tax deficiency against that corporation as transferee of the Signal Gasoline Company in the amount of $468.33 for the year 1923. [R. 52, 74.] An appeal from this proposed deficiency was taken in the name of the Signal Gasoline Corporation and was docketed with the Board of Tax Appeals on November 19, 1928 (Docket No. 41532). [R. 52, 75.]

On December 12, 1928, a Decree of Dissolution was entered by the Superior Court of the State of California dissolving the Signal Gasoline Corporation upon its own application. This decree also ordered that [R. 87-88]:

> * * * S. B. Mosher, H. M. Mosher, O. W. March, Ross McCollum, C. LaV. Larzelere and R. H. Green are entitled to be, and are by the Court herein appointed, trustees for the stockholders of said corporation, with power and direction to settle all the

affairs of said corporation and to distribute and convey all the property of said corporation to each of said stockholders, in proportion to the number of shares owned and held by said stockholders when said distribution and conveyance shall be made * * *.

On December 28, 1929, the Commissioner of Internal Revenue mailed a letter to the Signal Gasoline Corporation proposing a tax deficiency against that corporation as transferee of the Signal Gasoline Company in the amount of $2,672.53 for the period ended September 11, 1924. [R. 52, 74.] An appeal from this proposed deficiency was taken in the name of the Signal Gasoline Corporation and was docketed with the Board of Tax Appeals on February 24, 1930 (Docket No. 47620). This petition in its first paragraph stated that "The petitioner is a dissolved corporation acting through its statutory trustees." The verification on the petition was signed by six persons and stated that they were "the statutory trustees of Signal Gasoline Corporation, a dissolved corporation." [R. 52, 75.]

Both petitions for redetermination above referred to were signed by Robert N. Miller and Melvin D. Wilson as attorneys for the petitioners. [R. 75.]

On February 16, 1932, the Board of Tax Appeals promulgated a single opinion with respect to both petitions. (25 B. T. A. 532.) The petitioner was described as "a dissolved California corporation, acting through its statutory trustees" and the opinion recited that "The petitioner concedes the tax liability [of the Signal Gasoline Company], but contends that it is not liable at law or in equity for the deficiency asserted." (25 B. T. A. 533.) The

Board concluded that transferee liability existed, and accordingly, no appeal having been taken, an assessment was made on September 10, 1932, against the Signal Gasoline Corporation in the amount of $468.33 plus interest of $227.96 for the taxable year 1923 and $2,672.53 plus interest of $1,200.70 for the period ended September 11, 1924. [R. 52-53, 88-90.]

B. Assessment Against Signal Gasoline Corporation for Its Own 1924 Taxes.

The Signal Gasoline Corporation filed its income tax return for the calendar year 1924 on or about May 13, 1925. [R. 53, 76.] On December 3, 1928, it signed and filed a consent extending the time for assessing any income taxes due for the year 1924 until December 31, 1929. [R. 54, 76, 91.]

On December 28, 1929, the Commissioner of Internal Revenue mailed a letter to the Signal Gasoline Corporation proposing a tax deficiency against that corporation in the amount of $14,137.05 for the period May 1 to December 31, 1924. This letter also proposed an assessment of other additional tax liabilities for the calendar years 1925 and 1926 which are not now in issue. [R. 54, 76-77.] An appeal from these proposed deficiencies was taken in the name of the Signal Gasoline Corporation and was docketed with the Board of Tax Appeals on or about February 24, 1930 (Docket No. 47621). This petition, signed by Robert N. Miller and Melvin D. Wilson as attorneys for the petitioners, in its first paragraph stated that "The petitioner is a dissolved California corporation acting through its statutory trustees." The petition was verified by the six trustees. [R. 55-56, 77-78.]

On March 14, 1932, the Board of Tax Appeals promulgated its opinion with respect to this petition. (25 B. T. A. 861.) The petitioner was described as "a dissolved California corporation acting through its statutory trustees." (25 B. T. A. 862.) The Board concluded that the proposed deficiencies were correct, and accordingly, no appeal having been taken with respect to the year 1924, an assessment was made on October 1, 1932, against the Signal Gasoline Corporation, in the amount of $14,137.05 plus interest of $6,080.77 for the period May 1 to December 31, 1924. [R. 56, 78, 97-99.]

The appellant urges that because the Signal Gasoline Corporation was dissolved in December, 1928, the proceedings before the Board of Tax Appeals and the subsequent assessments were null and void. The decisions of this and other courts establish that this contention is erroneous.

The Signal Gasoline Corporation was a California corporation. Prior to the general statutory revision of the California corporation law in 1931, Section 400 of the California Civil Code, as amended in 1921 [Appendix, *infra*], provided:

> Unless other persons are appointed by the court, the directors or managers of the affairs of a corporation at the time of its dissolution are trustees of the creditors and stockholders or members of the corporation dissolved, and have full powers to settle the affairs of the corporation, collect and pay outstanding debts, sell the assets thereof in such manner as the court shall direct, and distribute the proceeds of such sales and all other assets to the stockholders. Such trustees shall have authority to sue for and recover the debts and property of the corporation,

> and shall be jointly and severally personally liable to its creditors and stockholders or members, to the extent of its property and effects that shall come into their hands. * * *

When the Signal Gasoline Corporation was dissolved in 1928, a court order was entered as heretofore noted naming six trustees "with power and direction to settle all the affairs" of the corporation. All of the proceedings before the Board of Tax Appeals were prosecuted by these trustees who were clearly acting within the authority granted by the court. It therefore follows that such proceedings and the ensuing assessments adjudging the liabilities of the Signal Gasoline Corporation were valid. This conclusion is supported by the decision of this Court in *McPherson v. Commissioner,* 54 F. (2d) 751. There, a California corporation was dissolved in June, 1920. The trustees thereafter filed with the Commissioner of Internal Revenue a waiver of the time prescribed by law for making assessment of taxes against the corporation, and subsequently, within the proper time as extended, such assessment was made. Thereafter, in an action before the Board of Tax Appeals involving the transferee liability of these trustees individually they urged (p. 752):

> * * * (1) That the commissioner was not authorized under the law to make the deficiency assessment against a corporation that had been dissolved. (2) That the waiver extending the time within which the assessment might be made was invalid.
>
> * * * * * * * *

This court rejected both contentions saying (pp. 752, 753):

> Upon the dissolution of the corporation, the petitioner, together with Barthel, as directors of the corporation, became trustees, with the power and duty to adjust any unsettled affairs of the corporation; to collect its receivables and to pay its debts. Section 400 of the Civil Code of California, as it read during all of the time important to these tax proceedings, contained the following provisions:
>
> * * * * * * * *
>
> Those provisions do not limit the period during which the trustees shall continue to act. Hence, the implication is plain that they shall continue to act so long as any of the affairs of the dissolved corporation remain unsettled. *United States v. Laflin* (C. C. A.), 24 F. (2d) 683; *Havemeyer v. Superior Court*, 84 Cal. 327, 24 P. 121, 10 L. R. A. 627, 18 Am. St. Rep. 192. We find no reason to distinguish a case where trustees are acting to liquidate corporate affairs under the provisions of the California statute from those cases where liquidators are provided for to act in the corporate name. The corporation here concerned became liable for the tax during the year when it was functioning under its charter. That tax the commissioner was entitled to assess in some form, and whether he designated the corporation by name, as though it were still fully alive, or designated its estate under the term "a dissolved corporation," or designated it as "a dissolved corporation in the hands of trustees" seems to suggest a matter of form only and not one attended by substantial differences. It was necessary that the total amount of the tax which accrued against the corporation during its active existence be ascertained, in order that the tax might be

collected and the assets followed into whosoever hands they might be found. The fixing of the tax charge as it had accrued against the corporation was a necessary prerequisite to the ascertainment of the proportionate amounts due from the transferees of the assets. The former directors, acting as trustees, as the law provided they should act, were legally bound to take notice of the assessment proceedings of which they were given notice, following the return which they made to the commissioner.

* * * * * * * *

The validity of proceedings before the Board of Tax Appeals by a dissolved corporation through its trustees was also questioned in *Buzard v. Helvering,* 77 F. (2d) 391 (App. D. C.). There, the corporation had been dissolved in 1922 and subsequently a petition before the Board of Tax Appeals was filed for the corporation by an attorney authorized to do so by the corporate trustees. In sustaining the jurisdiction of the Board of Tax Appeals the court said (pp. 394, 395):

> Placing themselves squarely on the California law, as interpreted and pronounced by the Supreme Court of California in the Crossman case, petitioners say that, since the Navarro Lumber Company had been legally dissolved in 1922, it could not thereafter be served with process, could not appear, and could not itself admit anything, nor authorize anyone to do so for it. That, in these circumstances, all that was done in its behalf by its trustees in the matter of the appeal to the Board of Tax Appeals was a nullity, and there-

fore had no effect, and could have no effect, in exending the periods of limitations. * * * But, in our view, petitioners' premise is not sustainable on either of two grounds.

* * * * * * * * *

In taking the appeal, petitioners set out the authority on which they acted. They speak of themselves as the trustees of the lumber company "now in process of liquidation" and point to the statute of California for their authority to act. By reference to that statute (Civil Code, §400 as amended by St. Cal. 1921, c. 383, p. 574) we find that they have power to settle the affairs of the corporation, collect and pay outstanding debts, to sue and to be sued in relation to the debts and property of the corporation, and that they shall be jointly and severally liable to creditors to the extent of any property that shall come into their hands. It was in recognition of these duties and responsibilities that they filed the appeal. We think it cannot be urged that they were without authority, or the Board without jurisdiction. * * *

The case at bar does not involve the situation as in *G. M. Standifer Const. Corp. v. Commissioner,* 78 F. (2d) 285 (C. C. A. 9th), where an Oregon corporation, fully dissolved and without either statutory or judicially designated trustees, attempted nevertheless to litigate as a live corporation.[2] In the case at bar, to the contrary, the pro-

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[2]In *California Iron Yards Co. v. Commissioner,* 47 F. (2d) 514, 516, this Court referred to a California corporation dissolved in 1921 as "one of suspended animation," citing 7 *Cal. Jur.* 640; *Hanson v. Choynski,* 180 Cal. 275, 180 Pac. 816; *Rossi v. Caire,* 186 Cal. 544, 199 Pac. 1042; *Ransomme-Crummey Co. v. Superior Court,* 188 Cal. 393, 205 Pac. 446.

ceedings before the Board on behalf of the corporation were prosecuted by its duly authorized trustees. Had it so desired the corporation could have appealed to this Court for a review of the Board's decisions. As a matter of fact, it did appeal to this Court from the previously mentioned Board opinion in 25 B. T. A. 861 in so far as it determined the corporation's tax liabilities for 1925 and 1926. This Court reversed the Board's decision on the merits and remanded the case for recomputation. (*Signal Gasoline Corporation v. Commissioner,* 66 F. (2d) 886.) The Board made such recomputation, 30 B. T. A. 568. Again the corporation effected an appeal to this Court at which time the Board's action was affirmed.

> *Signal Gasoline Corp. v. Commissioner,* 77 F. (2d) 728.[3]

The appellant's brief (p. 20) cites four decisions of the Board of Tax Appeals dealing with the effect of corporate dissolution upon Board proceedings. They are not in point since none of them was an action prosecuted by the properly constituted trustees.[4] Actually, the views of the Board of Tax Appeals with respect to dissolved California

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[3]In both appeals, the counsel for the Signal Gasoline Corporation was the present attorney for the appellant.

[4]*Sanborn Brothers v. Commissioner,* 14 B. T. A. 1059, was a purely officious suit by a stockholder of a dissolved California corporation. *S. Hirsch Distilling Co. v. Commissioner,* 14 B. T. A. 1073, concerned a Missouri corporation totally dissolved without any person being authorized to maintain an action. The dismissal in *Iberville Wholesale Grocery Co. Ltd. v. Commissioner,* 15 B. T. A. 645, was entered because of lack of evidence as to the trustee's authority, but the case was reinstated when such authority was shown, 17 B. T. A. 235. *Union Plate & Wire Co. v. Commissioner,* 17 B. T. A. 1229, was also based upon the absence of a person authorized to act for the corporation.

corporations are in accord with the Government's views here expressed. See

Buzard v. Commissioner, 28 B. T. A. 247.

Apart from the foregoing reasons, it is clear that the appellant should not now be permitted to question the validity of the assessments made against the Signal Gasoline Corporation. The appellant as sole stockholder of that corporation acquired all its assets and, as will be shown hereafter, became liable at law as well as in equity for its unpaid taxes. The trustees of the Signal Gasoline Corporation were the officers and directors of the appellant and their actions before the Board of Tax Appeals were for the benefit of and in order to protect the interests of the appellant. In such circumstances, the appellant ought not to be permitted to assail the validity of the Board proceedings and the assessments against the Signal Gasoline Corporation. It has been so held in similar situations.

Warner Collieries Co. v. United States, 63 F. (2d) 34 (C. C. A. 6th);

Buzard v. Helvering, 77 F. (2d) 391 (App. D. C.).

II.

The Statute of Limitations Does Not Bar These Actions.

The appellant received the assets of the Signal Gasoline Corporation subject to the express condition that it assume payment of all taxes owing by the transferor. It thus became liable at law not only for the direct tax liabilities of the Signal Gasoline Corporation (*American Equitable Assur. Co. of New York v. Helvering,* 68 F. (2d) 46 (C. C. A. 2nd); *Helvering v. Wheeling Mold & Foundry Co.,* 71 F. (2d) 749 (C. C. A. 4th)), but also for the tax liabilities of that corporation as transferee of the Signal Gasoline Company.

> *Continental Baking Co. v. Helvering,* 75 F. (2d) 243 (App. D. C.).

The appellant also became liable in equity for such taxes since as sole stockholder of the Signal Gasoline Corporation it acquired all the assets of that corporation.

> *United States v. Updike,* 281 U. S. 489;
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> *Phillips v. Commissioner,* 283 U. S. 589;
>
> *Pann v. United States,* 44 F. (2d) 321 (C. C. A. 9th).

Prior to the Revenue Act of 1926 such transferee liability could only be enforced by an action at law or by a bill in equity. That act, however, by Section 280(a)(1) provided that transferee liability could be enforced in the same manner and subject to the same limitations as that

of any delinquent taxpayer. Section 280(a)(1) reads as follows:[5]

> (a) The amounts of the following liabilities shall, except as hereinafter in this section provided. be assessed, collected, and paid in the same manner and subject to the same provisions and limitations as in the case of a deficiency in a tax imposed by this title (including the provisions in case of delinquency in payment after notice and demand, the provisions authorizing distraint and proceedings in court for collection, and the provisions prohibiting claims and suits for refunds):
>
> (1) The liability, at law or in equity, of a transferee of property of a taxpayer, in respect of the tax (including interest, additional amounts, and additions to the tax provided by law) imposed upon the taxpayer by this title or by any prior income, excess-profits, or war-profits tax Act.
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> * * * * * * * * *

The time within which assessments could be made against transferees was specified in Section 280(b)(c) and (d). [Appendix, *infra.*] It will be observed that these subsections which followed Section 280(a) are concerned with limitations upon assessments and not upon collections. As the Supreme Court has stated, "the suc-

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[5]Section 280 of the Revenue Act of 1926 is applicable to taxes imposed by the Revenue Act of 1926 and prior acts. Essentially similar provisions applicable to taxes imposed by subsequent Revenue Acts may be found in Section 311 of the Revenue Acts of 1928, 1932, 1934, 1936, 1938 and Section 311 of the Internal Revenue Code. (See, also, amendments effected by Section 814 of the Revenue Act of 1938.)

ceeding paragraphs contain provisions of limitation in respect of assessment, they contain none in respect of collection."

United States v. Updike, 281 U. S. 489, 494.

In order to ascertain the period of limitation upon collection against a transferee it is necessary to refer to Section 280(a) which states that the liability of a transferee shall be "* * * collected * * * in the same manner and subject to the same provisions and limitations as in the case of a deficiency in tax imposed by this title (including * * * the provisions authorizing * * * proceedings in court for collection * * *)." This section therefore incorporates the limitation provision which is normally applicable to all taxpayers, *i. e.,* Section 278(d). This interrelation of Section 280(a) and Section 278(d) was expressly recognized in *United States v. Updike, supra.* In that case the Court concluded (p. 494) that "the effect of the language above quoted from Section 280 is to read into that section and make applicable to the transferee equally with the original taxpayer, the provision of Section 278(d) in relation to the period of limitation for the collection of a tax."

Section 278(d) of the Revenue Act of 1926 provides:

> Where the assessment of any income, excess-profits, or war-profits tax imposed by this title or by prior Act of Congress has been made (whether before or after the enactment of this Act) within the statutory period of limitation properly applicable thereto, such tax may be collected by distraint or by a proceeding

> in court (begun before or after the enactment of this Act), but only if begun (1) within six years after the assessment of the tax, or (2) prior to the expiration of any period for collection agreed upon in writing by the Commissioner and the taxpayer.

Thus, a six-year limitation was placed upon proceedings in court to collect tax assessments. The applicability of this limitation to the consolidated cases at bar will now be discussed.

Case No. 1461-Y (Originally 1461-R J)—This action seeks to recover from the appellant the amount of taxes assessed for the year 1924 against the Signal Gasoline Corporation as an original taxpayer. The assessment was made on October 1, 1932. [R. 56.] This suit was instituted September 9, 1938. [R. 15.] Since the action was brought within six years after the assessment against the Signal Gasoline Corporation, it was timely.

Revenue Act of 1926, Secs. 280(a) and 278(d).

See

United States v. Updike, supra;

United States v. Adams, 92 F. (2d) 395 (C. C. A. 5th).

Case No. 1460-Y—This action seeks to recover from the appellant the amount of taxes for the years 1923 and 1924 assessed against the Signal Gasoline Corporation as transferee of the Signal Gasoline Company. These assessments were made on September 10, 1932. [R. 53.] This suit was instituted September 9, 1938. [R. 9.] Since the

action was brought within six years after the assessments against the Signal Gasoline Corporation, it too was timely.

Revenue Act of 1926, Secs. 280(a) and 278(d).

See

City Nat. Bank v. Commissioner, 55 F. (2d) 1073 (C. C. A. 5th).

The only difference between these two actions is that the former is to recover upon an assessment against the Signal Gasoline Corporation for an original tax liability and the latter is to recover upon an assessment against the Signal Gasoline Corporation for a transferee tax liability. The Revenue Act makes no distinction between these two situations and establishes a single rule of limitation with respect to both. If the liability of a transferee is not made the subject of an assessment then suit for collection from the transferee may be instituted within six years after the assessment was made against the transferor. (See *United States v. Adams, supra.*) If the liability of the transferee is reduced to an assessment, then suit for collection from the transferee may be instituted within six years from the date of that assessment.[6] See

City Nat. Bank v. Commissioner, supra.

Case No. 1461-Y presents no problem. The Signal Gasoline Corporation was liable for 1924 taxes. The assessment for such taxes was timely made and within six

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[6]The appellant in fact concedes that a suit against a transferee can be instituted within six years after a transferee assessment has been made against him. It views the assessment of October 1, 1932, as in effect a transferee assessment against the trustees of the Signal Gasoline Corporation and admits (Br. 28) that "The Government had six years from October 1, 1932, to sue the trustees * * *."

years thereafter suit for collection was instituted against the appellant.

Case No. 1460-Y presents a slight variation from the usual case since the tax assessments against the Signal Gasoline Corporation were for transferee liabilities. It is equally clear, however, that the six-year limitation applies. Had the Signal Gasoline Corporation retained assets, the Commissioner of Internal Revenue could have sued that corporation within six years after the transferee assessments were made against it. To urge that this period of collection can be reduced by a voluntary transfer of the assets of the Signal Gasoline Corporation to its sole stockholder is to urge a patent form of tax evasion. The Signal Gasoline Corporation with respect to its transferee liabilities was a "taxpayer." The Supreme Court has said that "it puts no undue strain upon the word 'taxpayer' to bring within its meaning that person whose property * * * is subjected to the burden." (*United States v. Updike, supra,* p. 494. *Cf. City of New York v. Feiring,* decided by the Supreme Court May 26, 1941.) The appellant as transferee of the Signal Gasoline Corporation was a transferee of a taxpayer within the meaning of Section 280(a), and therefore could be sued for the collection of any assessment which had been made within six years against the Signal Gasoline Corporation.

The appellant's case rests upon *United States v. Continental Bank,* 305 U. S. 398. In that case in 1926, James Duggan petitioned the Board of Tax Appeals to redetermine certain proposed tax deficiencies asserted to be due from him as transferee of corporate assets. In March, 1929, he died but no personal representative of the testator or other person applied for substitution of a party to carry

on the proceeding and none was ordered. The Board's order sustaining the Commissioner was entered in January, 1931. On February 14, 1931, the Commissioner of Internal Revenue made a jeopardy assessment against James Duggan. The administrator of his estate distributed the assets to various beneficiaries including the Continental National Bank and Trust Company as trustee. The United States thereafter instituted suit against these beneficiaries to recover the amount of the tax. In denying the Government's right to a recovery, the Supreme Court (Mr. Justice Stone and Mr. Justice Black dissenting) said that the statute was not broad enough to impose on "* * * testamentary transferees of the estate of the testator * * * any liability on account of the assessment against the testator" (p. 404) and moreover concluded that for stated reasons the assessment against the testator had not been made in time.

It seems clear that the decision in the *Continental* case has no bearing on case No. 1461-Y. That suit is simply a suit against a transferee to recover an original tax liability of the transferor which had been assessed against the transferor. It is not a suit against a transferee of a transferee as the appellant urges on the theory that the assessment was in effect against the trustees as transferees of the Signal Gasoline Corporation. The assessment was a determination of the tax liability of the Signal Gasoline Corporation[7] which under Section 281(b) of the Revenue

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[7]See *McPherson v. Commissioner*, 54 F. (2d) 751, 752 (C. C. A. 9th); *United States v. Russell*, 22 F. (2d) 249, 251 (C. C. A. 5th).

Act of 1926 was to be collected from the assets of the corporation. Those assets were taken over by the appellant and this suit instituted against it within six years from the date of the assessment.

Nor is there any validity in the assertion that the *Continental* case controls in case No. 1460-Y. Here, the assessments against the Signal Gasoline Corporation were made timely, and whatever may be the propriety of denyiny recovery against the testamentary transferees of an individual taxpayer does not apply where the transferee is a corporation which as sole stockholder voluntarily acquired the assets of another corporation. This is particularly true where as here there was an express assumption of the tax liabilities of the transferor. The *Continental* case does not establish the broad ruling contended for by the appellant and no valid reason has been suggested for extending it beyond its facts. Certainly, it should not be extended to cases involving the acquisition of corporate assets by its sole stockholder, another corporation.

Where justice requires it the courts will not be bound by the fiction of the corporate entity.[8] Here, the transferor and the transferee were separate entities in legal form only. The appellant was the sole stockholder of the Signal Gasoline Corporation. Its officers and directors were the trustees of the Signal Gasoline Corporation. In the transfer of the assets of the Signal Gasoline Corporation to the

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[8]This principle has already been applied to the appellant in other litigation. See *Wiethoff v. Refining Properties, Ltd.*, 8 Cal. App. (2d) 64, 68.

appellant, there was at no time any change in either beneficial interest or control. It is therefore particularly appropriate that this Court should not permit the appellant to maintain before it the legal fiction of two distinct entities for the purpose of setting up the defense of the statute of limitations and to avoid the payment of taxes justly due. *Cf.*

Higgins v. Smith, 308 U. S. 473.

Conclusion.

It is submitted that the decision of the District Court was correct and therefore that the judgment should be affirmed.

Respectfully submitted,

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July 22, 1941.

APPENDIX.

Statutes.

Revenue Act of 1926, c. 27, 44 Stat. 9:

PERIOD OF LIMITATION UPON ASSESSMENT AND COLLECTION OF TAX.

Sec. 277. (a) Except as provided in section 278—

(2) The amount of income, excess-profits, and war-profits taxes imposed by the Revenue Act of 1921, and by such Act as amended, for the taxable year 1921 and succeeding taxable years, and the amount of income taxes imposed by the Revenue Act of 1924, shall be assessed within four years after the return was filed, and no proceeding in court without assessment for the collection of such taxes shall be begun after the expiration of such period.

* * * * * * * * *

(b) The running of the statute of limitations provided in this section or in section 278 on the making of assessments and the beginning of distraint or a proceeding in court for collection, in respect of any deficiency, shall (after the mailing of a notice under subdivision (a) of section 274) be suspended for the period during which the Commissioner is prohibited from making the assessment or beginning distraint or a proceeding in court, and for 60 days thereafter.

* * * * * * * * *

Sec. 278. * * *

(d) Where the assessment of any income, excess-profits, or war-profits tax imposed by this title or by prior Act of Congress has been made (whether before or after the enactment of this Act) within the statutory period of limitation properly applicable

thereto, such tax may be collected by distraint or by a proceeding in court (begun before or after the enactment of this Act), but only if begun (1) within six years after the assessment of the tax, or (2) prior to the expiration of any period for collection agreed upon in writing by the Commissioner and the taxpayer.

* * * * * * * * *

CLAIMS AGAINST TRANSFERRED ASSETS.

Sec. 280. (a) The amounts of the following liabilities shall, except as hereinafter in this section provided, be assessed, collected, and paid in the same manner and subject to the same provisions and limitations as in the case of a deficiency in a tax imposed by this title (including the provisions in case of delinquency in payment after notice and demand, the provisions authorizing distraint and proceedings in court for collection, and the provisions prohibiting claims and suit for refunds):

(1) The liability, at law or in equity, of a transferee of property of a taxpayer, in respect of the tax (including interest, additional amounts, and additions to the tax provided by law) imposed upon the taxpayer by this title or by any prior income, excess-profits, or war-profits tax Act.

(2) The liability of a fiduciary under section 3467 of the Revised Statutes in respect of the payment of any such tax from the estate of the taxpayer. Any such liability may be either as to the amount of tax shown on the return or as to any deficiency in tax.

(b) The period of limitation for assessment of any such liability of a transferee or fiduciary shall be as follows:

(1) Within one year after the expiration of the period of limitation for assessment against the taxpayer; or

(2) If the period of limitation for assessment against the taxpayer expired before the enactment of this Act but assessment against the taxpayer was made within such period,—then within six years after the making of such assessment against the taxpayer, but in no case later than one year after the enactment of this Act.

(3) If a court proceeding against the taxpayer for the collection of the tax has been begun within either of the above periods,—then within one year after return of execution in such proceeding.

(c) For the purposes of this section, if the taxpayer is deceased, or in the case of a corporation, has terminated its existence, the period of limitation for assessment against the taxpayer shall be the period that would be in effect had the death or termination of existence not occurred.

(d) The running of the period of limitation upon the assessment of the liability of a transferee or fiduciary shall, after the mailing of the notice under subdivision (a) of section 274 to the transferee or fiduciary, be suspended for the period during which the Commissioner is prohibited from making the assessment in respect of the liability of the transferee or fiduciary (and in any event, if a proceeding in respect of the liability is placed on the docket of the Board, until the decision of the Board becomes final), and for 60 days thereafter. (As amended by Sec. 505 of the Revenue Act of 1928.)

(e) This section shall not apply to any suit or other proceeding for the enforcement of the liability of a

transferee or fiduciary pending at the time of the enactment of this Act.

(f) As used in this section, the term "transferee" includes heir, legatee, devisee, and distributee.

FIDUCIARIES.

Section 281. * * *

(b) Upon notice to the Commissioner that any person is acting in a fiduciary capacity for a person subject to the liability specified in section 280, the fiduciary shall assume, on behalf of such person, the powers, rights, duties, and privileges of such person under such section (except that the liability shall be collected from the estate of such person), until notice is given that the fiduciary capacity has terminated.

* * * * * * * * *

California Civil Code as amended in 1921 (Kerr's Biennial Supplement, Annotated (1921), p. 465):

§400. DIRECTORS TRUSTEES OF CREDITORS, ON DISSOLUTION. Unless other persons are appointed by the court, the directors or managers of the affairs of a corporation at the time of its dissolution are trustees of the creditors and stockholders or members of the corporation dissolved, and have full powers to settled the affairs of the corporation, collect and pay outstanding debts, sell the assets thereof in such manner as the court shall direct, and distribute the proceeds of such sales and all other assets to the stockholders. Such trustees shall have authority to sue for and recover the debts and property of the corporation, and shall be jointly and severally personally liable to its creditors and stockholders or members, to the extent of its property and effects that shall come into their hands. * * *

No. 9813

IN THE

United States Circuit Court of Appeals

FOR THE NINTH CIRCUIT

SIGNAL OIL AND GAS COMPANY,

Appellant,

vs.

UNITED STATES OF AMERICA,

Appellee.

REPLY BRIEF FOR APPELLANT.

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REPLY BRIEF FOR APPELLANT.

I.

The Alleged Assessments Against Signal Gasoline Corporation Are Invalid.

Appellee cites no authority for its contention that the alleged assessments against Signal Gasoline Corporation were valid, excepting *McPherson v. Commissioner,* 54 Fed. (2d) 751, and *Buzard v. Helvering,* 77 Fed. (2d) 391.

As shown in appellant's opening brief, the *McPherson* case has been substantially overruled by this Court in *G. M. Standifer Construction Corp. v. Commissioner,* 78 Fed. (2d) 285, and rendered inapplicable to cases of

this type by the decision of the Supreme Court of the United States in *United States v. Continental National Bank & Trust Co.,* 305 U. S. 398.

The decision in *Buzard v. Helvering, supra,* is not in point at all, as there the proceedings in the Court of Appeals of the District of Columbia were by the statutory trustees as an entity and not by the corporation. See page 29 of appellant's opening brief.

On page 15 of its brief, appellee attempts to distinguish the case of *G. M. Standifer Construction Corp v. Commissioner, supra,* by stating that it was a fully dissolved corporation and without either statutory or judicially designated trustee, attempting, nevertheless, to litigate as a live corporation. That decision establishes a principle which appellant is relying on in this proceeding, namely, that when a corporation is dissolved and there is no statutory provision for continuing its corporate existence for any purpose, the dissolution of the corporation absolutely destroys it and all pending actions against the corporation are abated, and the corporation is thereafter incapable of acting or suing or being sued. See, also, *Oklahoma Natural Gas Co. v. State of Oklahoma,* 273 U. S. 257; *Crossman v. Vivienda Water Co.,* 150 Cal. 575, 89 Pac. 335, and *Brandon v. Umpqua Lumber Co.,* 166 Cal. 322, 136 Pac. 62, 7 Cal. Jur. 37-38.

The only difference between the *Standifer* case and the case at bar was that in the *Standifer* case the corporation continued in existence for five years, acting through its statutory trustees, after which it became entirely de-

stroyed, whereas in the case at bar, Signal Gasoline Corporation became destroyed immediately, but a new entity, its statutory trustees, was set up to take over the assets and liabilities. In each case, however, the corporation was destroyed, one at the end of five years and the other immediately.

On page 17 of its brief, appellee contends that appellant should be estopped from questioning the validity of the alleged assessments made against the Signal Gasoline Corporation. Appellee cites *Warner Colleries Co. v. United States,* 63 Fed. (2d) 34; *Buzard v. Helvering,* 77 Fed. (2d) 391.

In *Warner Colleries Co. v. United States, supra,* there were grounds for estoppel, whereas in the case at bar, there are no grounds for estoppel, as is shown by the fact that appellee has not squarely met the issue of estoppel. It has merely asked for the benefits of the doctrine of estoppel, without squarely meeting the issue or discussing the subject.

In *Warner Colleries Co. v. United States, supra,* a petition was filed by the dissolved corporation in its name, which petition was signed by persons who designated themselves as officers of the corporation, and the corporate seal was used. No statement was made in the petition that the company had been dissolved. Before the Board of Tax Appeals, also, the representatives of the corporation signed a stipulation, substantially reducing the taxes and agreeing that the taxes could be assessed against the corporation. Furthermore, the successor corporation which was

held liable for the tax, ratified the acts of its directors who signed the petition as officers of the dissolved corporation. Consequently, the Board could safely proceed on the theory that it was dealing with an existing corporation. Naturally that corporation or its successors could not contend that the Board was put on notice of the dissolution, and therefore could not contend that the proceedings were void. There was a clear case of estoppel on the basis of the facts involved.

As to *Buzard v. Helvering,* also cited by appellant on page 17, as authority for its estoppel plea, as has been previously shown the proceeding there was not against the corporation but against the statutory trustees as an entity, hence it is not a case which holds that an assessment can be made against a dissolved corporation because of the estoppel of its representatives. No suit of a corporation was involved, but it was a suit against the new entities, the statutory trustees.

II.

The Statute of Limitations Bars These Actions.

Appellant, on pages 18 to 23, inclusive, of its brief, merely points out a few matters which have always been understood in this case, namely, that appellant, except for the statute of limitations, is liable under law and equity for the additional taxes (if any) of Signal Gasoline Company and Signal Gasoline Corporation; that Section 280 of the Revenue Act of 1926 has nothing to do with suits without assessment; that the statute of limitations involved in the case at bar is Section 278 (d) of the Revenue Act of 1926; that if the alleged assessments made against Signal Gasoline Corporation were valid, as to case No. 1460-Y, the only question remaining is whether under Section 278 (d), the Government had six years after an assessment against a first transferee to sue a second transferee, and as to case No. 1461-Y, one question is the same as that stated with respect to case No. 1460-Y, and the further question is whether the statutory trustees of Signal Gasoline Corporation constituted the first transferees and appellant the second transferee of the assets of Signal Gasoline Corporation.

Case No. 1460-Y.

As to case No. 1460-Y, involving the taxes of Signal Gasoline Company, allegedly assessed against Signal Gasoline Corporation, and sought to be recovered in suit against appellant, the appellant sets up two defenses.

The appellant contends that the suit is barred for two reasons: First, that the alleged assessment against Signal

Gasoline Corporation was void; and second, that even if it was valid, it did not give the Government six years within which to sue appellant, because appellant is the transferee of the transferee of Signal Gasoline Company, and the case of *United States v. Continental National Bank & Trust Co., supra,* decided that Section 278 (d) does not give the Government six years within which to sue the transferee of a transferee.

The appellee is apparently not satisfied with the decision of the Supreme Court in *United States v. Continental National Bank & Trust Co.,* seemingly casting some doubt upon its present validity, on pages 24 and 25 of the brief. Appellee also, on page 25 of its brief, says the *Continental* case is not applicable, except to transferees of an individual taxpayer, and bases this contention again on its plea of estoppel. But of course there was as strong an equity in favor of the Government in the *United States v. Continental* case as there is in the case at bar; that is to say, the tax was obviously owed in the *Continental* case, but the court held that the Government was delinquent in proceeding against the proper transferees. The tax that the Government lost there was huge, amounting to over $295,000 with interest. Furthermore, the original taxpayer there, as in the case at bar, was a corporation.

The appellee says, on page 25 of its brief, that the fiction of corporate entity will be disregarded if justice requires it. The appellee impliedly contends that justice does not require the use of the statute of limitations specifically enacted by Congress. As a matter of fact, justice requires that there be a repose with respect to litigation, and that principle is just as important to the proper working of the national fisc as is the collection

of a tax in an individual case. The citizens of the United States have to have confidence in the taxing authorities and the courts construing tax statutes, including confidence in the protection afforded by the statute of limitations, or they will rely upon their own ingenuity for self protection, thereby requiring a great deal more tax litigation, which would be ruinous to the national fisc. No government can afford to have litigation with respect to but a very small percentage of its cases, but if people lose confidence in the tax tribunals to fairly decide all questions of taxation, including questions of the statute of limitations, the result would be very detrimental to the Government.

It need not be pointed out to this Court that there is a statute of limitations on suits for recovering taxes overpaid, nor that the Government very diligently invokes the statute of limitations on every possible occasion. Naturally, the Government pleads the statute of limitations in those cases because justice requires it.

What is justice for the Government is justice for the taxpayer. Furthermore, taxes are not determined by the application of equitable principles, but by the application of the statutory language. An exception is made in cases calling for the doctrine of estoppel, but the facts of the present case do not invoke the principle of estoppel in the Government's favor.

Appellee says, on pages 25 and 26 of its brief, that the various corporate entities involved in this matter, were separate entities in legal form only, and that in transferring the assets from one to another there was no change at any time in either beneficial interests or control, and that the Court should disregard the legal fiction of separate entities, and prevent appellant from setting up the defense of the statute of limitations.

This again is a plea for estoppel without squarely meeting the issues involved in the question of estoppel, and without proving the various elements of estoppel to be present. The question of estoppel is gone into quite extensively in appellant's opening brief. The facts were all fully and clearly known by the appellee, within proper time for it to act. The corporations were all separate and tax liabilities were separately recognized by appellee; the various procedures in the audit of the return were entirely separate, and appellee is simply trying to put the blame on others for its own delinquencies. When the Government brings suit in 1938 for 1923 and 1924 taxes of corporations which had long been dissolved, of which dissolution the Government had full and timely notice, it would seem that it was a proper case for the application of the statute of limitations to put a repose to the said litigation.

As can be seen from any daily paper, the stock of appellant is listed upon the stock exchange and it may be assumed that its stockholders constantly change from time to time. It would be entirely inequitable to hold appellant liable for the tax liabilities of other corporations which accrued seventeen and eighteen years ago, on account of transfers which occurred eleven years ago, because of the acts of a few of appellant's stockholders, who were trustees of predecessor corporation, taken approximately ten years ago.

Appellee, on page 25 of its brief, cites the case of *Wiethoff v. Refining Properties, Ltd.,* 8 Cal. App. (2d) 64, as authority for the proposition that the Court should look through the fiction of corporate entities.

The cited case has no bearing on the situation involved in the case at bar. Entirely different issues were involved.

Furthermore, none of the companies involved in the case at bar, except appellant, were involved in the cited case. Other corporations involved in the cited case were Signal Oil and Gas Company of California, Pacific Service Stations and Refining Properties, Ltd., all apparently organized after Signal Gasoline Company and Signal Gasoline Corporation had been dissolved. The situation there involved several companies which were in existence at the same time. In the case at bar, the situation involved corporations which had been dissolved before, or about the time appellant was organized.

Appellant also cites, on page 26 of its brief, *Higgins v. Smith,* 308 U. S. 473, as authority for the proposition that separate corporate entities in the case at bar should be disregarded.

But in *Higgins v. Smith, supra,* the question was the deductibility of a loss purportedly sustained by the sole stockholder of a corporation, on the sale of securities to that company. There a jury had found that the corporation was created for tax savings purposes of the sole stockholder and was simply an agent of the taxpayer. There, also, the issue involved was the matter of a deduction against gross income. The courts have uniformly held that in claiming deductions, the statute must be strictly construed and the taxpayer must prove that his claim comes strictly within the statutory language.

In the case of the statute of limitations, however, the courts have ruled that questions of doubt must be ruled strictly against the Government, and in favor of the taxpayer. See pages 31 and 32 of appellant's opening brief.

In *Higgins v. Smith,* the taxpayer deliberately sought to save taxes by setting up a corporation and had that

subject uppermost in his mind in making transactions with it. In the case at bar, all transactions involved were regular business transactions involving a substantial number of persons with no deliberate attempt or consciousness of tax saving, or tax avoidance.

CASE No. 1461-Y.

The principal contentions of the appellant with respect to Case No. 1461-Y can be restated as follows:

1. That the alleged assessment made against Signal Gasoline Corporation was invalid; hence no tax was shown to be due, and no six-year period for bringing suit was started by the void assessment;

2. That even if it were valid, it would not give the Government six years within which to sue a transferee of a transferee;

3. Appellant is the transferee of a transferee of the assets of Signal Gasoline Corporation, because its statutory trustees were the first transferees of the assets of Signal Gasoline Corporation, and appellant received the assets from the first transferees, namely, the statutory trustees of Signal Gasoline Corporation.

Appellee does not cite any authority in answering the last contention listed above. As shown on pages 27 to 30, inclusive, of appellant's opening brief, the statutory trustees of Signal Gasoline Corporation constituted the first transferees. Consequently, appellant was the second transferee of the assets of Signal Gasoline Corporation and under *United States v. Continental National Bank*

and Trust Co., supra, the Government did not have six years after the alleged assessment was made against the first transferee to sue appellant, the second transferee of the assets of Signal Gasoline Corporation.

As pointed out in appellant's opening brief, the appellee made two mistakes of law and is now trying to shift the loss and blame to other persons. These mistakes were the following: First, after having been advised that Signal Gasoline Corporation had been dissolved, it failed to properly construe Section 400 of the California Civil Code, to the effect that the dissolution of a California corporation completely destroyed it. Appellee thereafter continued to regard the dissolved corporation as being in existence, instead of dealing with its statutory trustees as a separate entity; second, appellee construed Section 278 (d) of the Revenue Act of 1926 as giving it a six-year period within which to sue the transferee of a transferee of the assets of a taxpayer. This was erroneous, as shown by the decision of the Supreme Court of the United States, in *United States v. Continental National Bank and Trust Co., supra.*

The appellee made these mistakes of law and took the wrong procedure and the present suits are barred by the statute of limitations, and appellee should not be permitted to do what this Court barred it from doing in *Van Antwerp v. United States,* 92 Fed. (2d) 871. There this Court said:

> "* * * It was incumbent upon the Commissioner to reaudit her income for that year as soon as the

> Malcom decision advised him of his error. This for the protection of the Treasury, which otherwise would lose what she owed, because of the Government's wrong interpretation of the law. Fourteen months remained for such reaudit and deficiency assessment, during which the Government did nothing. Having failed to do so, it seeks to transfer the loss from that neglect to the appellant taxpayer."

In conclusion it is submitted that the decisions for the District Court were incorrect and that the judgments should be reversed.

Dated: July 31, 1941.

Respectfully submitted,

MELVIN D. WILSON,
Attorney for Appellant.

NO. 9817

United States

Circuit Court of Appeals

For the Ninth Circuit.

ISIDORE WINKLEMAN, alleged bankrupt,
Appellant,

vs.

T. OGAMI, MESAL BAG COMPANY, PORTLAND BAG and METAL COMPANY and ENKE'S CITY DYE WORKS, INC.,
Appellees.

Transcript of Record

Upon Appeal from the District Court of the United States for the District of Oregon.

PARKER PRINTING COMPANY, 545 SANSOME STREET, SAN FRANCISCO

No. 9817

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[Clerk's Note: When deemed likely to be of an important nature, errors or doubtful matters appearing in the original certified record are printed literally in italic; and, likewise, cancelled matter appearing in the original certified record is printed and cancelled herein accordingly. When possible, an omission from the text is indicated by printing in italic the two words between which the omission seems to occur.]

APPEARANCES

MOE M. TONKON,
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Portland, Oregon
Attorney for Appellant

WILLIS WEST,
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Portland, Oregon
Attorney for Appellees

In the District Court of the United States
For the District of Oregon

No. B 24917

In the Matter of

ISIDORE WINKLEMAN,

Alleged Bankrupt.

AGREED STATEMENT OF CASE UNDER RULE 76, RULES OF CIVIL PROCEDURE

On May 18, 1940, an involuntary petition in bankruptcy was filed in the above-entitled court against the above named alleged bankrupt. Said petition had only one petitioning creditor, T. Ogami, and averred that the alleged bankrupt had creditors less than twelve in number. The alleged bankrupt filed an answer to the creditor's petition, setting out in conformance with the statute, the names of all of his creditors. Whereupon there was filed petitions in intervention by Portland Bag & Metal Company and Messel Bag Co., two creditors of the alleged bankrupt. The intervening petitioning creditors in their respective petitions alleged the same acts of bankruptcy as were alleged in the original petition.

The alleged bankrupt having filed his answer to the intervening petitions, the cause came on for pre-trial, at which time the alleged bankrupt, with leave of court, amended by interlineation his answers to the original petition and the intervening

petitions to provide, "That the petitioning creditor and the intervening petitioning creditors, and each of them, have received preferences which they have not returned or offered to return in their petitions".

Prior to the continued hearing upon the pre-trial, Enke's City Dye Works Inc., a creditor of the alleged bankrupt, filed its petition in intervention, setting forth the same acts of bankruptcy alleged in the original petition and the intervening petitions of the Messel Bag Co., and Portland Bag & Metal Company.

The issues, in accordance with the pre-trial order, were:

(1) Whether or not the respective claims of T. Ogami, Messel Bag Co., and Portland Bag & Metal Company, petitioning creditors and intervening petitioning creditors in this cause, are provable claims under the Acts of Congress relating to bankruptcy, and whether or not said creditors, or any of them, have received preferences and have not offered to return same.

(2) Whether or not the Acts of Bankruptcy as alleged in the petition in this cause constitute acts of bankruptcy within the purview of the Acts of Congress relating to bankruptcy.

At the trial of this cause a stipulation was made between the parties admitting the provability of the claim of Enke City Dye Works, one of the intervening petitioning creditors, and that said creditor was qualified under the provisions of the

statute to join in the petition as a petitioning creditor. No evidence was offered to support the claim of Messel Bag Company, one of the intervening petitioning creditors. Evidence was offered in support of the alleged bankrupt's claim that T. Ogami and the Portland Bag & Metal Company, petitioning creditor and intervening creditor received preferences and failed to offer to return them.

The trial court rendered its opinion and found that whether the petitioning creditors and intervening creditor had received preferences and had failed to offer to return them was not an issue in the cause, and accordingly it did not consider evidence offered in support thereof. It found further that the allegations contained in the original petition and the intervening petitions of Portland Bag & Metal Company and Enke City Dye Works had been proven and based thereon made its order of adjudication on March 5, 1941, a copy of which order is attached hereto as Exhibit A.

Notice of appeal was served upon the attorney for the petitioning creditors and filed with the Clerk of the United States District Court for the District of Oregon on April 4, 1941, a copy of said notice of appeal as filed is hereto attached and marked Exhibit B.

The appellant (alleged bankrupt) upon the appeal will contend:

(1) That the court erred in failing to consider and determine whether T. Ogami and the Portland Bag & Metal Company, petitioning creditor and intervening creditor received preferences and offered to return them.

(2) The court erred in its conclusion that a preferred creditor may be a petitioning creditor of an involuntary petition in bankruptcy without returning or offering to return the preference received by said creditor in its petition.

The parties hereto agree that the foregoing statement of the case may be considered by the appellate court as an agreed statement of the case in the within cause, and essential to a decision of the questions and points arising upon the appeal herein.

WILLIS WEST,
Attorney for Original and Petitioning Creditors.

MOE M. TONKON,
Attorney for Alleged Bankrupt.

Dated at Portland, Oregon, this 5th day of May, 1941.

EXHIBIT A

District Court of the United States
for the
..... District of Oregon
——— Division

Bankruptcy File No. B-24917

In the Matter of

ISIDORE WINKLEMAN

Bankrupt.

ADJUDICATION OF BANKRUPTCY.

At Portland, in said district, on the 5th day of March, 1941.

The petition of T. Ogami, filed on May 18, 1940, Mesal Bag Company, and Portland Bag and Metal Company, filed on September 23, 1940, and Enke's City Dye Works, Inc., filed on December 18, 1940 that Isidore Winkleman be adjudged a bankrupt under the act of Congress relating to bankruptcy, having been heard and duly considered;

It is adjudged that the said Isidore Winkleman is a bankrupt under the act of Congress relating to bankruptcy.

CLAUDE McCOLLOCH,
District Judge.

[Endorsed]: Filed March 6, 1941. G. H. Marsh, Clerk. L. S. Rogers, Deputy.

EXHIBIT B

In the District Court of the United States
For the District of Oregon

No. B 24917

In the Matter of

ISIDORE WINKLEMAN,

Alleged Bankrupt.

NOTICE OF APPEAL

Comes now Isidore Winkleman, alleged bankrupt herein, and gives notice that he appeals to the United States Circuit Court of Appeals for the Ninth Circuit from that certain order of adjudication and the whole thereof, duly made and entered in the above entitled cause by the Honorable Claude McColloch, Judge of the United States District Court for the District of Oregon, on March 5, 1941.

(Sgd) MOE M. TONKON,
Attorney for Isidore Winkleman,
Alleged Bankrupt.

Due service of the within Notice of Appeal is hereby accepted this 4th day of March, 1941, by receiving a copy thereof, duly certified to as such by Moe M. Tonkon, attorney for Alleged Bankrupt.

(Sgd) WILLIS WEST,
Attorney for Petitioning and
Intervening Creditors.

[Endorsed]: Filed April 4, 1941. G. H. Marsh, Clerk. By L. S. Rogers, Deputy.

The foregoing statement of the case is a true and correct statement of a sufficient portion of the pleadings, evidence and proceedings in the within cause to fully present to the appellate court the questions and points raised on the appeal herein.

Dated at Portland, Oregon, this 6th day of May, 1941.

CLAUDE McCOLLOCH,
District Judge.

[Endorsed]: Filed May 6, 1941. G. H. Marsh, Clerk. By L. S. Rogers, Deputy.

United States of America,
District of Oregon—ss.

I, G. H. Marsh, Clerk of the United States District Court for the District of Oregon, do hereby certify that the foregoing copy of Agreed Statement of Case under Rule 76, Rules of Civil Procedure, in Cause No. B24917, in the Matter of Isidore Winkleman, Alleged Bankrupt, has been by me compared with the original thereof, and that it is a correct transcript therefrom, and of the whole of such original, as the same appears of record and on file at my office and in my custody.

In testimony whereof I have hereunto set my hand and affixed the seal of said court at Portland, in said District, this 7th day of May, 1941.

[Seal] G. H. MARSH,
Clerk,

By L. S. ROGERS,
Deputy Clerk.

[Endorsed]: No. 9817. United States Circuit Court of Appeals for the Ninth Circuit. Isidore Winkleman, alleged bankrupt, Appellant, vs. T. Ogami, Mesal Bag Company, Portland Bag and Metal Company and Enke's City Dye Works, Inc., Appellees. Transcript of Record. Upon Appeal from the District Court of the United States for the District of Oregon.

Filed May 10, 1941.

PAUL P. O'BRIEN,

Clerk of the United States Circuit Court of Appeals for the Ninth Circuit.

In the United States Circuit Court of Appeals
For the Ninth Circuit

No. 9817

In the Matter of

ISIDORE WINKLEMAN,

Alleged Bankrupt.

STATEMENT OF POINTS UPON WHICH APPELLANT INTENDS TO RELY UPON APPEAL AND DESIGNATION OF PARTS OF RECORD TO BE USED IN CONSIDERATION THEREOF.

Comes now Isidore Winkleman, appellant herein, and respectfully represents to this Honorable Court

that he intends to rely upon the following points upon the appeal herein:

(1) That the District Court erred in failing to consider and determine whether T. Ogami and the Portland Bag & Metal Company, petitioning creditor and intervening creditor received preferences and offered to return them.

(2) The District Court erred in its conclusion that a preferred creditor may be one of the petitioning creditors in an involuntary petition in bankruptcy without returning or offering to return the preference received by said creditor in its petition.

In support of the foregoing points upon which appellant intends to rely upon on the appeal herein, the court is respectfully referred to the Agreed Statement of Case under Rule 76, Rules of Civil Procedure, duly agreed to by the parties hereto and certified to by the Honorable Claude McColloch, United States District Judge for the District of Oregon, and filed in the within cause.

MOE M. TONKON,
Attorney for Appellant.

Dated at Portland, Oregon this 13th day of May, 1941.

State of Oregon,
County of Multnomah—ss.

Due service of the within Statement of Points upon which Appellant intends to rely upon appeal is hereby accepted in Multnomah County, Oregon, this 13th day of May, 1941, by receiving a copy thereof, duly certified to as such by Moe M. Tonkon, attorney for alleged bankrupt.

WILLIS WEST,
Attorney for Petitioning and
Intervening Creditors.

[Endorsed]: Filed May 15, 1941. Paul P. O'Brien, Clerk.

No. 9817

United States
Circuit Court of Appeals
For the Ninth Circuit

ISIDORE WINKLEMAN, alleged bankrupt,
Appellant,

vs.

T. OGAMI, MESAL BAG COMPANY, PORTLAND BAG AND METAL COMPANY and ENKE'S CITY DYE WORKS, INC.,
Appellees.

Appellant's Brief

Upon Appeal from the District Court of the United States, for the District of Oregon.

MOE M. TONKON,
Attorney for Appellant.

WILLIS WEST,
Attorney for Appellees.

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No. 9817

United States
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ISIDORE WINKLEMAN, alleged bankrupt,
Appellant,

vs.

T. OGAMI, MESAL BAG COMPANY, PORTLAND BAG AND METAL COMPANY and ENKE'S CITY DYE WORKS, INC.,
Appellees.

Appellant's Brief

Upon Appeal from the District Court of the United States, for the District of Oregon.

STATEMENT OF JURISDICTION

This is an appeal from an order of the United States District Court for the District of Oregon, adjudicating the appellant a bankrupt upon an involuntary petition. (Tr. 2).

The Acts of Congress relating to Bankruptcy, commonly known as the Bankruptcy Act, specifically give to the several "Courts of Bankruptcy" jurisdiction to adjudge persons bankrupt.

Courts of Bankruptcy are defined by the Bankruptcy Act:

> "Courts of Bankruptcy" shall include the District Courts of the United States and of the Territories and possessions to which this title is or may hereafter be applicable, and the District Court of the United States for the District of Columbia;" *Title* 11, *Section* 1 (10) *U. S. C. A. as amended.*

The jurisdiction of the several District Courts of the United States in Bankruptcy is provided in the Bankruptcy Act as follows:

> "The Courts of the United States hereinbefore defined as courts of bankruptcy are hereby created courts of bankruptcy and are hereby invested, within their respective territorial limits as now established or as they may be hereafter changed, with such jurisdiction at law, and in equity as will enable them to exercise original jurisdiction in proceedings under this title, in vacation, in chambers, and during their respective terms, as they are now or may be hereafter held, to—
>
> (1) Adjudge persons bankrupt who have had their principal place of business, resided or had their domicile within their respective territorial jurisdictions for the preceding six months, or for a longer portion of the

preceding six months than in any other jurisdiction, or who do not have their principal place of business, reside, or have their domicile within the United States, but have property within their jurisdictions, or who have been adjudged bankrupts by courts of competent jurisdiction without the United States, and have property within their jurisdictions;" *Title* 11, *Section* 11, *a, U. S. C. A. as amended.*

The Circuit Court of Appeals by virtue of the following express provisions of the Bankruptcy Act, has appellate jurisdiction from the several courts of bankruptcy in their respective jurisdictions in proceedings or controversies in bankruptcy.

"The Circuit Court of Appeals of the United States and the United States Court of Appeals for the District of Columbia, in vacation, in chambers, and during their respective terms, as now or as they may be hereafter held, are hereby invested with appellate jurisdiction from the several courts of bankruptcy in their respective jurisdictions in proceedings in bankruptcy, either interlocutory or final, and in controversies arising in proceedings in bankruptcy, to review, affirm, revise, or reverse, both in matters of law and in matters of fact: Provided, however, That the jurisdiction upon appeal from a judgment on a verdict rendered by a jury, shall extend to matters of law only: Provided further, That when any order, decree, or judgment involves less than $500, an appeal therefrom may be taken only upon allowance of the appellate court." *Title* 11, *Section* 47, *a, U. S. C. A. as amended.*

In the present case the jurisdiction of the United States District Court for the District of Oregon and the appellate jurisdiction of this court, in light of the foregoing provisions of the statute, is clear.

STATEMENT OF THE CASE

An involuntary petition in bankruptcy was filed in the United States District Court for the District of Oregon against Isidore Winkleman, the alleged bankrupt (Appellant herein). The petition was filed solely by T. Ogami and contained averments that the alleged bankrupt had creditors less than twelve in number. (Tr. 2). Pursuant to the statute, the alleged bankrupt filed his answer to the involuntary petition and scheduled his creditors, which schedule showed that his creditors exceeded twelve in number. Subsequently there were filed petitions in intervention by the Portland Bag & Metal Company, Mesal Bag Company and Enke's City Dye Works, Inc., who were other creditors of the alleged bankrupt, and who joined in the petition. (Tr. 2). The alleged bankrupt filed his answer to each of the intervening petitions and contended "that the original petitioning creditor and the intervening petitioning creditors, and each of them, had received preferences which they had not returned or offered to return in their petitions." (Tr. 3).

At the trial it was stipulated that Enke's City Dye

Works, Inc., one of the intervening petitioning creditors, was qualified to join in the petition as a petitioning creditor and has a provable claim. No evidence was offered to support the provability of the claim of Mesal Bag Company or that said creditor was qualified to join in the petition. Evidence was offered in support of the alleged bankrupt's claim that T. Ogami, the original petitioning creditor, and the Portland Bag & Metal Company, the intervening petitioning creditor, had received voidable preferences and failed to offer to return them in the petitions. (Tr. 3).

The trial court rendered its opinion and held that whether the petitioning creditor and intervening creditor had received preferences and had failed to offer to return them was not an issue in the cause and, accordingly, it did not consider the evidence offered in support thereof. (Tr. 4). The court further held that the allegations contained in the original petition filed by T. Ogami and the intervening petitions of Portland Bag & Metal Company and Enke's City Dye Works, Inc., had been sustained by evidence and that in accordance with the statute three or more creditors had joined in the petition, and based upon its holding it made and entered its order of adjudication on March 5, 1941. (Tr. 6).

From this order of adjudication the alleged bankrupt, feeling aggrieved, has commenced the present appeal. (Tr. 7).

There has been filed as the record in this cause an Agreed Statement of the Case under Rule 76, Rules of Civil Procedure, duly agreed to by all the parties hereto and certified to by the United States District Judge as being a complete statement of a sufficient portion of the pleadings, evidence and proceedings in the within cause to fully present to this court the questions and points raised on the appeal herein. (Tr. 2-8).

THE QUESTION INVOLVED

The sole question involved is whether or not a creditor who has received a voidable preference can be counted in an involuntary petition in bankruptcy as one of the petitioning creditors without surrendering or offering to surrender the preference received by him.

SPECIFICATION OF ERROR TO BE RELIED ON

The District Court erred in making and entering its order adjudicating the appellant a bankrupt without first determining from the evidence whether or not T. Ogami, original petitioning creditor, and Portland Bag & Metal Company, intervening petitioning creditor, received preferences and offered to surrender said preferences received by them.

POINTS AND AUTHORITIES

A creditor who has received a voidable preference cannot be counted as one of the petitioning creditors upon an involuntary petition without surrendering or offering to surrender the preference received by him.

In re Fishblatt, 125 Fed. 986; 11 Am. B. R. 204.

Stevens v. Nave McCord Co., 150 Fed. 71; 17 Am. B. R. 609.

Matter of John F. Murphy, 225 Fed. 392, 35 Am. B. R. 635.

Matter of Standard-Detroit Tractor Co., 275 Fed. 952; 47 Am. B. R. 642.

In the Matter of Macklem, 22 Fed. (2d) 426; 10 Am. R. B. (N. S.) 550.

Matter of Phillips & Co., Inc., 28 Fed. (2d) 299; 12 Am. B. R. (N. S.) 312.

Brehme v. Watson, 67 Fed. (2d) 359; 24 Am. B. R. (N. S.) 166.

Vol. 1 *Remington on Bankruptcy,* Page 368, section 258.

Vol. 2 *Collier on Bankruptcy,* Page 1217, 1218.

Section 59b, Bankruptcy Act.

Section 59c, Bankruptcy Act.

ARGUMENT

In his answer the alleged bankrupt contended that the petitioning creditors, and each of them, had received preferences and had not surrendered them or offered to surrender them in their petitions. At the trial of this cause,

it was admitted that one of the creditors, Enke's City Dye Works, Inc., had a provable claim and was qualified to join in the petition. Another creditor, the Mesal Bag Company, did not offer any proof in support of its claim and its qualification as a petitioning creditor, and therefore cannot be considered as having joined in the petition. (Tr. 3). Evidence was submitted to support the alleged bankrupt's contention that the other two creditors who had joined in the petition, T. Ogami and Portland Bag & Metal Company, had each received preferences within four months prior to the filing of the petition. The appellant contended that these preferences were voidable under the Bankruptcy Act and that each of these creditors had failed to surrender such preferences or failed to offer to surrender such preferences in their petition. Accordingly, if the appellant's contention that the above described creditors had received preferences is sustained, these creditors having received voidable preferences, are not to be counted in determining the number of creditors who have joined in the petition. If appellant prevails, the petition must fail as there remains only one qualified creditor, the Enke's City Dye Works, Inc. The District Court heard the evidence offered to prove that the petitioning creditors had received preferences and that said creditors had refused to surrender or offer to surrender them, but in its opinion the court held that this matter was not an issue in the proceeding.

The rule has been well settled by the weight of authority existing prior to the enactment of the Chandler Act that a creditor who holds a preference, while he may join in the petition if he has a provable claim, cannot be counted as one of the required number of creditors who may join in the petition without first surrendering or offering to surrender in the petition the preference so received by him. The most recent expression of this rule is found *In the Matter of Macklem,* 22 Fed. (2d) 426; 10 Am. B. R. (N. S.) 550. In this decision it appears that an involuntary petition for an adjudication of a bankrupt was filed by three creditors. The alleged bankrupt answered the petition and, among other things, contended that the petitioning creditors had been preferred within four months of the filing of the petition and that accordingly they were disqualified to act as petitioning creditors. The court sustaining this contention in its opinion, held: (Italics ours).

> "As to the matter of disqualification of the three petitioning creditors, the Bankruptcy Act, section 59 (b) provides that 'three or more creditors who have provable claims against any person * * * may file a petition to have him adjudged a bankrupt.' Under some of the decisions, 'provable' is held to mean any claim which might be proved, whether preferred or not; while other cases hold that it is the aquivalent of 'allowable'. See In re Standard-Detroit Tractor Co., (D. C. Mich.), 47 Am. B. R. 642, 275 F. 952, 954. *But the weight of authority is that a creditor who has received a voidable preference may still join in the petition, though he may*

not be counted as one of the required three petitioning creditors unless he surrenders his preference. Stevens v. Nave McCord Co., (C.C.A., 8th Cir.). 17 Am. B. R. 609, 150 F. 71; In re Gillette (D. C., N. Y.), 5 Am. B. R. 119, 104 F. 769; Canute S. S. Co. v. Pittsburgh Coal Co., 263 U. S. 244, 2 Am. B. R. (N. S.) 231, 44 S. Ct. 67, 68 L. ed. 287; In re Cooper (D. C. Mass.) 7 Am. B. R. (N. S.) 643, 12 F. (2d) 485. As was said in the Stevens case:

"* * * The evil of preferences which the bankrupt law was enacted to remove, the remedy of an equal distribution of the property of the bankrupt which it was passed to provide, the prohibition of the use of their claims by preferred creditors until they surrender them, which the act contains, the general scope of the law and all its provisions read and considered together, and the duty to give to it a rational and sensible interpretation, have forced our minds to the conclusion that it was the intention of Congress that creditors who hold voidable preferences should not be counted either for or against the petition for an adjudication in bankruptcy until they surrender their preferences. This intention, thus deduced, must therefore prevail over the technical rules of construction which counsel for the appellees invoke. *The result is: A creditor who holds a voidable preference has a provable claim in the sense that he may make and file the formal proof thereof specified by the bankruptcy law; but he may not procure an allowance of his claim, he may not vote at a creditors' meeting, and he may not obtain any advantage from his claim in the bankruptcy proceeding before he surrenders his preference.*

Such a preferred creditor may present or may join in a petition for an adjudication of bankruptcy. *But he*

may not be counted for the petition unless he surrenders his preference before the adjudication. In re Hornstein (D. C. N. Y.), 10 Am. B. R. 308, 122 F. 266, 273, 277; In re Gillette (D. C. N. Y.) 5 Am. B. R. 119, 104 F. 769."

For additional authorities in support of the foregoing rule, see: *Matter of Phillips & Co Inc.,* 12 Am. B. R. (N. S.) 312; 28 Fed. (2d) 299; *Stevens v. Nave McCord Co.,* 150 F. 71; 17 Am. B. R. 609; *Matter of Standard-Detroit Tractor Co.,* 275 Fed. 952; 47 Am. B. R. 642; *Matter of John F. Murphy,* 225 Fed. 392; 35 Am. B. R. 635; *In re Fishblatt,* 125 Fed. 986; 11 Am. B. R. 204; *Vol.* 1 *Remington on Bankruptcy,* page 368, Section 258; *Vol.* 2 *Collier on Bankruptcy,* Page 1217, 1218.

In Volume 1, *Remington on Bankruptcy,* 1940 Supplement, page 40, the author states that this court has impliedly held in *Brehme v. Watson,* 67 Fed. (2d) 359, 24 Am. B. R. (N. S.) 166, that a creditor holding an attachment lien secured within four months immediately preceding the filing of a petition in bankruptcy cannot join in such petition without first surrendering his lien.

The foregoing rule has been well established prior to the enactment of the Chandler Act, and said rule has not been altered or changed by the amendatory provisions of this Act. A comparative analysis of the pertinent sections of the Bankruptcy Act as they existed prior to the Chandler Act and after the amendment by virtue of said act discloses: (Italics indicate Chandler Act amendment)

CHANDLER ACT

(Section 59b, Bankruptcy Act)

"Three or more creditors who have provable claims *fixed as to liability and liquidated as to amount* against any person which amount in the aggregrate in excess of the value of securities held by them, if any, to $500 or over; or if all of the creditors of such person are less than twelve in number, then one of such creditors whose claim equals such amount may file a petition to have him adjudged a bankrupt."

* * *

(Section 59e, Bankruptcy Act)

"In computing the number of creditors of a bankrupt for the purpose of determining how many creditors must join in the petition, there shall not be counted

(1) such creditors as were employed by the bankrupt at the time of the filing of the petition;

(2) creditors who are relatives of the bankrupt, *or, if the bankrupt is a corporation, creditors who are stockholders or members, officers or members of the board of directors or trustees or of other similar controlling bodies of such bankrupt corporation;*

(3) *creditors who have participated, directly or indirectly, in the act of bankruptcy charged in the petition;*

(4) *secured creditors whose claims are fully secured; and*

(5) *creditors who have received preferences, liens, or transfers void or voidable under this Act.*"

OLD ACT

(Section 59b, Bankruptcy Act)

"Three or more creditors who have provable claims against any person which amount in the aggregate, in excess of the value of securities held by them, if any, to five hundred dollars or over, or if all of the creditors of such person are less than twelve in number, then one of such creditors whose claim equals such amount may file a petition to have him adjudged a bankrupt."

* * *

(Section 59e, Bankruptcy Act)

"In computing the number of creditors of a bankrupt for the purpose of determining how many creditors must join in the petition, such creditors as were employed by him at the time of the filing of the petition or are related to him by consanguinity or affinity within the third degree, as determined by the common law, and have not joined in the petition, shall not be counted."

It appears clear that the only amendment to Section 59b of the Bankruptcy Act is the requirement that the claim of the creditor joining in the petition must be fixed as to liability and liquidated as to amount. This amendment was apparently made to avoid the necessity of liquidating, estimating and determining claims of petitioners which might be contingent or unliquidated and thus the trial of a contested petition would be expedited. It thus appears that the amendment to Section 59b does not alter or change the rule that existed under the old act.

Section 59e, subsection (5) of the Chandler Act specifically excludes in the count to determine whether the requisite number of creditors have joined in the petition "creditors who have received preferences * * *." The Chandler Act now clarifies and codifies the rule that had been established prior thereto. It clearly expresses the intent of Congress to require preferred creditors to surrender their preferences prior to being counted as petitioning creditors. It is interesting to note that in an early leading case enunciating this rule prior to the amended act (*Stevens v. Nave McCord Co.*, 150 F. 71; 17 Am. B. R. 609), there was a complete and thorough discussion of the reasons why a preferred creditor should not be counted in a petition without first surrendering his preference.

In the court's opinion it states that one of the arguments advanced by one of the preferred petitioning creditors was that the act then existing did not in any manner preclude preferred creditors from being counted in determining whether the requisite number of creditors had joined in the petition. Notwithstanding this contention the court adhered to the rule that the preferred creditor must first surrender or offer to surrender his preference before he may be counted as a petitioning creditor. Furthermore, under the amended Bankruptcy Act (Chandler Act) this argument is set at rest by virtue of the specific statutory exclusion of creditors who hold preferences from being counted as one of the required number who may join in a petition. (Section 59e (5) Bankruptcy Act).

The spirit and intent of the Bankruptcy Act throughout is to afford an equal distribution of the property of the bankrupt to all creditors, and it is only reasonable to expect that one who has received such a preference should surrender the preference or offer to surrender the same if he desires in any manner to seek the aid of the Act. If a preferred creditor may join in a petition without surrendering or offering to surrender his preference, he has an advantage over other creditors which advantage he retains in spite of the fact that he is at-

tempting to invoke the aid of the Bankruptcy Act in adjudicating the debtor a bankrupt. A bankruptcy proceeding is an equitable proceeding. Preferred creditors refusing to surrender their preference run afoul of the ancient equitable maxim *"he who comes into equity must come with clean hands."* It is manifestly unfair to subject all of the debtor's other creditors to the risk of having their debts discharged without receiving a ratable distribution of the debtor's assets. The act in many instances specifically precludes preferred creditors from acquiring certain rights thereunder without surrendering their preferences. For example, a preferred creditor cannot vote at meetings of creditors (Section 56b Bankruptcy Act); preferred creditors cannot have their claims allowed unless they surrender their preferences (Section 57g Bankruptcy Act).

CONCLUSION

The rule as adopted by many courts requiring a preferred creditor to surrender or offer to surrender his preference before being counted as a petitioning creditor is well established. The Chandler Act does not in any manner alter or change this rule and as a matter of fact codifies the old rule. Accordingly, it should be clear that

the District Court erred in failing to determine whether the petitioning creditors had received preferences. The order of adjudication should be reversed.

Respectfully submitted,

MOE M. TONKON,

Attorney for Appellant.

No. 9817

In the United States Circuit Court of Appeals

For the Ninth Circuit

ISIDORE WINKLEMAN, alleged bankrupt,
Appellant,

vs.

T. OGAMI, MESAL BAG COMPANY, Portland Bag and Metal Company and Enke's City Dye Works, Inc.,
Appellees.

APPELLEES' BRIEF

Upon Appeal from the District Court of the United States, for the District of Oregon.

MOE M. TONKON,
Attorney for Appellant.
WILLIS WEST,
Attorney for Appellees.

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Appellees.

APPELLEES' BRIEF

Upon Appeal from the District Court of the United States, for the District of Oregon.

OPENING STATEMENT

This case is before the court upon an agreed statement of the case which is set forth in the transcript of record. It is for the decision of this court whether the lower court erred in refusing to consider as an issue at the hearing on the involuntary petition in bankruptcy filed by the appellees whether or not any of the petitioning creditors had received preferences and refused to surrender them.

The appellant attempted to make an issue out of certain alleged preferences claimed to have been received by the petitioning creditors, and contended it was for the lower court to determine whether such preferences had been received or not, and if so, such petitioning creditors would be disqualified if they refused to surrender or offer to surrender such alleged preferences.

It is admitted that the alleged bankrupt had more than twelve creditors at the time of the filing of the involuntary petition in bankruptcy, and three qualified creditors were required to support the petition for an order of adjudication. The lower court held that under the law, no issue could be made as to the qualification of such three creditors on the question as to whether or not they had received preferences and failed or refused to surrender them. This appeal raises a question which, in the belief of the writer, is squarely before an appellate court for the first time.

POINTS AND AUTHORITIES

THE ONLY QUALIFICATIONS OF A PETITIONING CREDITOR ARE THAT HE SHALL HAVE A PROVABLE CLAIM FIXED AS TO LIABILITY AND LIQUIDATED AS TO AMOUNT.

Sec. 59 (b) Bankruptcy Act, as amended (11 U.S.C.A. § 95).

In re Hornstein, 122 Fed. 266, 10 Am. B. R. 308.

ARGUMENT

The appellant has not cited any statutory authority setting forth any greater qualifications that must be met by a petitioning creditor, other than as set forth in Section 59 (b) of the Bankruptcy Act, supra.

The sole qualifications of the petitioning creditor are set out in that subsection of the Bankruptcy Act, and no provision of the Act expressly disqualifies a petitioning creditor merely because he may have received a voidable preference. The petitioning creditor carries the burden of establishing he holds a provable claim under the Bankruptcy Act, and this does not necessarily mean an "allowable" claim.

A distinction must be recognized between the words "provable" and "allowable". A claim may be provable and not be allowable. If a petitioning creditor was required to prove that he had an allowable claim, then the question of surrendering a preference may be considered by the court in determining such creditor's qualifications.

It is the position of the appellants that the lower court was charged with the duty to determine whether or not the claim was both provable and allowable. A very interesting discussion of the distinction between a provable claim and allowable claim is found in the case of In re Hornstein, 122 Fed. 266, in which the court determined that a prov-

able claim was not necessarily an allowable claim and that it was not incumbent upon a petitioning creditor to establish an allowable claim in order to maintain an involuntary petition in bankruptcy.

A PETITIONING CREDITOR HAVING A VOIDABLE PREFERENCE MAY FILE OR JOIN IN AN INVOLUNTARY PETITION IN BANKRUPTCY.

Section 59, Bankruptcy Act, as amended (11 U.S.C.A. § 95).
In re Hornstein, 122 Fed. 266 (275), 10 Am. B. R. 308.
In re Macklem, 22 Fed. (2d) 426, 10 Am. B. R. (N.S.) 550.
Stevens v. Nave-M'Cord Mercantile Co., 150 Fed. 71, 17 Am. B. R. 609.

ARGUMENT

It is admitted by the appellant, and supported by ample authority, that no petitioning creditor is disqualified to file or join in an involuntary petition in bankruptcy merely because he holds a voidable preference. The jurisdiction of the court over the proceedings in bankruptcy is established by the proper petition of such a creditor. The appellant contends that although the court has jurisdiction of the proceedings, no order of adjudication can be made until the petitioning creditor holding a preference has surrendered, or offered to surrender, such preference. No provision of the Bankruptcy Act, as amended, expressly terminates the jurisdiction of

the bankruptcy court to enter an order of adjudication upon failure of the petitioning creditor to surrender his preference.

A CREDITOR RECEIVING A PREFERENCE CAN QUALIFY AS ONE OF THE NECESSARY PETITIONING CREDITORS IN AN INVOLUNTARY PETITION IN BANKRUPTCY WITHOUT SURRENDERING, OR OFFERING TO SURRENDER, AN ALLEGED VOIDABLE PREFERENCE.

> In re Automatic Typewriter & Serv. Co., 271 Fed. 1 (Circuit Court of Appeals, 2nd Circuit, 1921).

A search of the authorities on the above point indicates that the question involved in this appeal is helped very little by existing precedents. The only case decided in an appellate court that sheds any light on this point is the case of In re Automatic Typewriter & Serv. Co., supra. In this case, the Circuit Court of Appeals refused to reverse the Federal District Court for the Southern District of New York when it upheld an involuntary petition in bankruptcy filed by a petitioning creditor holding an attachment lien against the bankrupt's property. The bankrupt had contended in its answer that the petitioning creditor had received a preferential payment on account of the attachment and therefore such creditor was disqualified to maintain its petition. The court said:

> "Furthermore, the preferred creditor who files a claim may surrender his preference at any time before the claim is allowed. This he need not do before the filing of the claim. We think the court below committed no error in refusing to dismiss the petition in bankruptcy because of this." (p. 4)

Although the above case involving an attachment lien is not precisely in point with the instant case, where the preference is based upon an alleged payment to the creditor, still the reason in both situations for not dismissing the petition on account of the alleged preference, is present. No advantage is held by a petitioning creditor holding a preferential payment over other creditors. The mere joining in the petition gives him no further rights. He should not be required to surrender, or offer to surrender, an alleged preference before adjudication when he may honestly believe he holds no preferential payment, and since the decree of adjudication in involuntary bankruptcy is not res adjudicata as to the amount or validity of the claims of petitioning creditors when subsequently presented for allowance.

> In re Continental Engine Co. (C.C.A.), 234 F. 58.
> In re Harper (D.C.N.Y.), 175 F. 412.
> Remington on Bankruptcy (4th ed.) Secs. 530 and 966.

One of the main purposes of the bankruptcy laws is to protect creditors against losses through preferential transfers. The filing of involuntary peti-

tions in bankruptcy is the method by which the creditors bring the debtor under the jurisdiction of the bankruptcy court to avoid such preferential transfers. A preferred creditor should be no less qualified by reason of his preference than any other creditor when he requests the court to adjudicate the debtor a bankrupt.

A creditor receiving a preference can have no advantage, and seeks no advantage, when he joins with other petitioning creditors to have the bankrupt's property subjected to the jurisdiction of the Bankruptcy Court. In fact, by joining in the petition, he has done the very thing that may bring about the subsequent surrender of any preference that he may hold. If he did not join in the petition no adjudication may ever take place, and the preference he holds would be retained by him without any right on the part of other creditors to demand a surrender thereof.

By joining in the petition, the petitioning creditor alleged to have received a preference, has willingly and voluntarily submitted himself to the jurisdiction of the court and thereby puts the machinery in motion whereby his claim may be subsequently affected by failure to surrender a preference, found to be such, at the time of the allowance of his claim.

Considerable has been said in appellant's brief relative to the rights of a preferred creditor, insofar as participating in the benefits of all the bankruptcy proceedings, until he has surrendered his

preferences. The appellant contends that a petitioning creditor must surrender, or offer to surrender, his preference, before he may be counted as a petitioning creditor, and cites Section 59 (b) of the Bankruptcy Act, as amended. Sub-section (5) of the last quoted section in no way helps to solve the question before this court, as that sub-section as explained by sub-section (e) only provides that creditors who have received preferences under the Act are not to be counted among the *total number of creditors* in determining whether there are more than eleven creditors necessitating the joining of three petitioning creditors to maintain an involuntary petition in bankruptcy.

Appellant cites a number of cases which deal only with the principle that creditors who have received a preference are not to be considered either for or against the petition in arriving at the total number of existing creditors as the basis for fixing the number of creditors that necessarily must join in the involuntary petition.

The principal cases cited by appellant in support of his contention are cases decided in the Federal District Courts, and it is only by careful analysis and consideration of these cases that one can recognize the error of the appellant in citing such cases as authority on the point involved.

The first case found, that in any way touches the point on review, is the case of

In re Gillette, 104 Fed. 769 (1900)

decided by the Western District Court of New York in 1900, wherein the petitioning creditor was also a judgment creditor and had received a certain preferential payment, and the court there refused to enter an order of adjudication until the petitioning judgment creditor had paid into the Clerk of the Court the amount of the preference. In arriving at the propriety of such a decision, the court did not predicate its decision upon any definite authority nor set forth any sound reason for requiring the preferred creditor to surrender his preference.

After this case followed:

In re Hornstein (1903), supra,

cited by the appellant. This was another District Court case which involved an attachment lien held by one of the petitioning creditors, and the court there approved the court's decision in: In re Gillette, and required the petitioning creditor to surrender the attachment lien before the order of adjudication could be entered. In this case the court failed to recognize that an order of adjudication would have resulted in a discharge of the attachment lien in the manner set forth in the case of In re Automatic Typewriter & Service Co., supra.

It is interesting to note that in the Hornstein case, the court said (p. 276):

> "Again, the attachment of these petitioners is not four months old, and hence will fall on an adjudication in bankruptcy."

In deciding that the preferred creditor could properly join as a petitioning creditor, the court, in the Hornstein case said further (p. 276):

> "Until the claim is 'proved' the court is powerless to 'allow' it, and until allowance is under consideration the question whether or not 'a preference' has been received cannot be determined by the court."

The court in that case pointed out the principal question before the court was whether the petitioner had a right to file a petition, and the holding that the attachment lien must be surrendered was purely obiter dictum by the court.

Following the Hornstein case, came the case of—

> In re Fishblate Clothing Co., 125 Fed. 986 (1903)

another District Court case cited by the appellant. There, the court, without citing any authority, merely made a finding that the petitioning creditor had received a preference which he would not voluntarily surrender, and therefore was disqualified from maintaining the petition. The petition was dismissed for other reasons besides the disqualification of the petitioner.

The next case, which is Stevens v. Nave McCord (1906), supra, decided in the Circuit Court of Appeals for the Eighth Circuit, and cited by appellant, is not truly decisive on the question involved in this appeal. The principal question before the court for decision was whether or not the preferred creditors

were to be counted in determining whether one or three creditors were required to maintain the petition, and there the court decided that creditors who received a voidable preference were not to be computed in determining how many must join in the petition, and it is important to note that the court expressly stated it was not deciding whether two of the petitioning creditors had a right to join with a third in a petition for adjudication. However, there is some dicta by the court in this case, appearing on page 76 of the reported case, that the petitioning creditor cannot be counted for the petition unless he surrenders his preference before the adjudication, citing: In re Hornstein, supra, and: In re Gillette, supra.

However, in this case it cannot be said any rule was established by this dicta as the court was principally concerned with the question as to the number of petitioning creditors required to support a petition in bankruptcy calculated upon the total number of creditors.

In the Matter of John F. Murphy, 225 Fed. 392 (1915), which is a District Court case cited by the appellant, should not be considered as an authority for the position taken by the appellant. The court simply took the dicta from the Stevens case without setting forth any reasons of its own and held that the preferential payment must be returned by depositing the same with the Clerk of the Court before an order of adjudication would be made.

The next case is: In re Standard-Detroit Tractor Co. (1921) 275 Fed. 952, 47 Am. B. R. 642, another District Court case, cited by appellant, which did not have before it the point in issue in this appeal, as it was conceded by the petitioning creditor that if he received a voidable preference he could not maintain his petition without surrendering, or offering to surrender, his preference before adjudication. Therein, the court said (p. 954):

> "It is therefore unnecessary to consider the question whether such a creditor may file such a petition without making a surrender of any voidable preference, previously obtained, a question which, in view of the distinction between the proving and the allowance of a claim in bankruptcy, and the consequent difference between the meaning of the terms 'provable' and 'allowable' is not free from difficulty, and cannot, in my opinion, be regarded as authoritatively decided."

Appellant next cites the case of: In re Cooper, 12 Fed. (2d) 485 (1926), which is another District Court case that merely decides that creditors who have received a preference are not to be counted in determining the number of creditors that must join in the petition in bankruptcy.

Next follows the case of In re Macklem, 22 Fed. (2d) 426, (1927), another District Court case cited by appellant. In this case, without supporting its views with any reasons, the court held the weight of authority is that a creditor who has received a voidable preference may not be counted as one of

the three required petitioning creditors, unless he surrenders his preference, citing the Stevens case, supra, In re Gillette, supra, In re Cooper, supra, Canute S. S. Co. v. Pittsburg Coal Co., 263 U.S. 244, 2 Am. B. R. (N.S.) 231, and In re Hornstein, supra. It cannot be said from an examination of such authorities cited that the decision In re Macklem, supra, is accurate precedent for the proposition contended for by the appellant.

The case of In re Phillips & Co., Inc., 28 Fed. (2d) 299 (1928), cited by the appellant, is a District Court case in which the court assumed the law to be as contended by the appellant, without citing any authority, and it does not appear that the decision in the case involved the question as to whether or not the petitioning creditors were qualified by reason of having received a preference.

The appellant cites the case of Brehme v. Watson, 67 Fed. (2d) 359, which is a case decided in the Circuit Court of Appeals for the Ninth Circuit, which did not have before it for decision the question involved in this appeal.

There is also cited the Supreme Court case of Canute Steamship Co. v. Pittsburg, etc., supra, which in no respect decided the question of law before this court.

A full consideration of the cases and authorities touching the points at issue can only lead to the conclusion that the District Courts have been con-

fused and misled by the early decisions of In re Gillette and In re Hornstein. And the dicta in the Stevens case further led the lower courts into deciding, without supporting reasons, that a petitioning creditor cannot secure an order of adjudication unless he surrenders any preference he may hold.

The question as to whether the jurisdiction of the bankrupt court was affected by the subsequent payment by the bankrupt of one of the petitioning creditors, was considered by the Circuit Court of Appeals of this Circuit in the case of Reed v. Thornton, 43 Fed. (2d) 813. Therein Judge Wilbur held that the jurisdiction of the court attached from the filing of a petition filed by three creditors, and that a subsequent payment by the bankrupt of some of the creditors could not deprive the court of jurisdiction.

It appears that if the acceptance of a preferential payment by a petitioning creditor after the filing of a petition did not affect the jurisdiction of the court, then the acceptance of a preferential payment by the petitioning creditor within four months prior to the filing of the petition would not deprive the court of jurisdiction to enter an order of adjudication by reason of any disqualifcation of such petitioning creditor.

CONCLUSION

A determination of the question before the court necessarily calls for some consideration of the effect of the Chandler Act upon the law of bankruptcy insofar as that act was adopted in 1938 for the purpose of clarifying certain provisions of the old bankruptcy act and eliminating the confusion of conflicting decisions, language ambiguities, etc.

The contentions of the appellant that the lower court was required to determine whether or not the three creditors were qualified on account of having received alleged preferences is not supported in any respect by any express statutory provisions of the Chandler Act.

A rule grew up under the decisions of the various courts that in computing whether one or three creditors are required to join in an involuntary petition in bankruptcy, the creditors holding preferences were not to be counted in arriving at the number required to join in the petition. This rule was firmly established by the courts and was based upon sound reasoning and good logic, and for the purpose of clarifying the bankruptcy law and making statutory that which had become law by "stare decisis", the Chandler Act added to Section 59 of the old bankruptcy act a specific provision eliminating creditors who had received voidable preferences under the Act from the total number of creditors to be counted in determining the number of creditors that must join in the petition.

It was out of the decisions establishing the foregoing rule that some of the courts recited the rule that is now being urged by the appellant as the law deciding the question of law in this appeal. However, it is interesting to note that the Chandler Act did not go so far as to set down by statute an express provision disqualifying a petitioning creditor holding a voidable preference which was not surrendered or offered to be surrendered prior to adjudication. It is reasonable to expect that if such was the law established by the decisions and if it was founded upon sound purpose, then the bankruptcy act would have been amended accordingly. For the one there is a reason, for the other there is none.

A decision in favor of the appellant herein will necessarily require this court to make some interpretation of the Bankruptcy Act based upon a good reason that a petitioning creditor holding a voidable preference is disqualified unless he surrenders his preference or offers to do so.

A petitioning creditor who holds a voidable preference holds no advantage over other creditors in law by failing to surrender or refusing to surrender his preference. Upon the entry of an order of adjudication the trustee may recover such preferences as may have been received by the creditor, and his claim will not be allowed until he surrenders his preference, and the rights of all creditors are fully protected and it would be a vain and useless thing

for the creditor alleged to be holding a voidable preference to require him to do that which the law requires him to do in order to preserve the jurisdiction of the court over the proceedings in bankruptcy.

The Circuit Court of Appeals has already recognized that the bankruptcy court is not ousted of jurisdiction when it is shown that a sole petitioning creditor is also holding an attachment lien acquired within four months of the filing of the petition.

> In re Automatic Typewriter & Service Co., supra.

The order of adjudication in such a case termiates the attachment lien and fixes the rights of the respective creditors to share in the property held as a preference. The identical rights are conferred upon the trustee to recover the property after an order of adjudication in those cases where a preferential payment has been received by one of the petitioning creditors.

It is respectfully submitted that neither the bankruptcy act as amended nor the decisions of the courts required that the lower court determine whether or not the petitioning creditors had received preference before entering an order of adjudication.

Respectfully submitted,

WILLIS WEST,
Attorney for Appellees.

No. 9817

United States
Circuit Court of Appeals
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Appellant,

vs.

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Appellant's Reply Brief

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Appellant's Reply Brief

Upon Appeal from the District Court of the United States, for the District of Oregon.

In the appellant's opening brief (Page 6) the question involved in the present appeal was presented and while the appellees in their opening statement apparently agree with the statement as to the issue involved as appears in the appellant's brief, the arguments advanced in the appellee's brief confuses the issue to some extent. The issue involved herein, simply stated, is whether or not a creditor who has received a voidable preference *can be counted* in an involuntary petition as one of the petitioning creditors

without surrendering or offering to surrender the preference received by him. The appellant in his opening brief has not questioned the right of such a creditor to join in the petition but the attack is made upon his qualification to be counted as one of the required number of petitioning creditors under the statute. In other words, appellant contends that if without counting a creditor who has received a voidable preference and who has not offered to surrender or return the preference in the petition, the number of creditors who have joined in the petition is less than three as required under Section 59b, then the petition must fail.

It is true, as contended by appellees, (Page 4, appellees' brief) that there is no provision of the Bankruptcy Act which expressly terminates the jurisdiction of the bankruptcy court to enter an order of adjudication upon failure of the petitioning creditor to surrender his preference. However, upon a reading of Section 59b of the Act it is clear that there must exist "three or more creditors" before the court has jurisdiction to entertain the petition, and under Section 59e it is further provided:

(Parenthetical matter and emphasis ours.)

> "In computing the number of creditors of the bankrupt for the purpose of determining how many creditors *must join in the petition,* (before the court has jurisdiction) there shall not be counted * * * * * *
>
> (5) creditors who have received preferences, liens, or transfers void or voidable under this Act."

The appellees have not cited any direct authority in their brief that was rendered prior to the enactment of the Chandler Act Amendment which in any manner conflicts with the rule adhered to in the many authorities cited in appellant's opening brief (Page 7, appellant's brief) upon the issue involved herein. Appellees have attempted to analyze these authorities but in each instance the analysis does not detract from the holdings of the opinions and the rule enunciated therein to the effect that a petitioning creditor cannot be counted in determining whether the required number of creditors have joined in the petition as provided under the Act, if he has failed to surrender or offer to surrender a voidable preference which he has received.

There has been cited, on Page 5 of appellees' brief, *In re Automatic Typewriter & Serv. Co.*, 271 Fed. 1, as appellees' authority upon the issue involved herein. This decision is not in any manner pertinent. It deals with a situation where an involuntary petition had been filed by a creditor who had in good faith obtained an attachment against the alleged bankrupt's property within four months prior to the filing of the petition. Objection was made that the creditor could not file the petition without first releasing his attachment. The facts were (as found in the opinion) that a motion had been made to vacate the attachment, which motion was granted, but a formal

order giving effect to the decision of the court was never entered. Accordingly, the warrant of attachment was not formally vacated at the time of the filing of the petition and the property of the alleged bankrupt was in the custody of the sheriff by virtue of the writ. Furthermore, this authority cites with approval *Stevens v. Nave-McCord Mercantile Co.,* 150 Fed. 71, 17 Am. B. R. 609, which case has been cited by the appellant in his opening brief at Pages 11 and 13. In the foregoing case cited by appellees appears the following extract from the *Stevens v. Nave-McCord Mercantile Co.,* case, supra (italics ours):

> "Such a preferred creditor may present or may join in a petition for an adjudication of bankruptcy. *But he may not be counted for the petition unless he surrenders his preference before the adjudication.*"

It is further submitted that the above mentioned Automatic Typewriter & Service Co. case cited by appellees is not applicable in the determination of the issue involved herein because of the subsequent enactment of the amended Section 59e, Subsection (5), which provides that "creditors who have received preferences, *liens* or transfers void or voidable under this Act" may not be counted in determining how many creditors must join in the petition.

There has been cited also by appellees on Page 14 of their brief the case of *Reed v. Thornton,* 43 Fed. (2d)

813, which case, it is submitted, is not applicable to the issue involved herein. In this decision it was held by this court that a payment by the bankrupt to some of the petitioning creditors after the filing of the petition could not deprive the court of jurisdiction. There can be no argument with this holding for the test is whether or *not at the time of the filing of the petition* the required number of qualified creditors had joined in said petition. Any act on the part of either the bankrupt or a creditor that subsequently disqualifies the creditor would certainly not destroy the court's jurisdiction which became fixed at the time the petition was filed. This is far different from the facts in the present matter because, at the time of the filing of the petition, two of the three required petitioning creditors, who joined in the petition had received voidable preferences and had not offered in the petition to surrender or return such voidable preferences. It is not contended by appellant that these creditors have received any preference subsequent to the time of the filing of the petition, but that the preferences they had received prior thereto which they have not offered to return disqualifies each of them from being counted as one of the necessary three creditors required under the provisions of the Bankruptcy Act.

Appellant in his opening brief contends that the rule established prior to the Chandler Act Amendment to Section 59b and Section 59e was to the effect that a creditor,

who had received a voidable preference, *could not be counted* as one of the required number of creditors without first surrendering or offering to surrender his preference and that said rule was codified by the foregoing amendment to the Bankruptcy Act. Appellees attempt to discount this rule, and the unequivocal provisions of the aforementioned sections of the Bankruptcy Act. It is their contention that these sections of the statute deal wholly with a formula for determining whether there exists less than twelve creditors to justify the filing of the petition by one creditor in lieu of three creditors in accordance with the provisions of the statute. However, upon a careful reading of the statute this argument must fail for Section 59e of the Bankruptcy Act specifically provides:

> "In computing the number of creditors of a bankrupt for the purpose of determining how many creditors must join in the petition there shall not be counted * * * *
>
> (5) creditors who have received preferences, liens, or transfers void or voidable under this Act."

The foregoing section of the statute does not reveal any limitation on its interpretation to being applicable solely for the purpose of determining what creditors may be counted in order to ascertain whether the alleged bankrupt has more or less than twelve in number of creditors. The foregoing provisions of the statute must be neces-

sarily interpreted as including a statutory qualification for those creditors who join with two or more creditors of an alleged bankrupt in filing a petition. If either or any of the creditors who so join are specifically excluded by the express provisions of Section 59e and there does not remain three creditors who may be counted, when the alleged bankrupt has twelve or more creditors, then the petition must necessarily fail.

Contrary to appellees' contention that the question on appeal is squarely before the appellate court for the first time (appellees' brief, page 2) appellant contends that the issue is settled by Section 59b and Section 59e (5) of the Chandler Act and the numerous sections and cogent reasons appearing therein cited in appellant's opening brief. This is indicated in the case of *Stevens v. Nave-McCord Co.,* supra, an extract from which case discussing the reasons for the ruling appears *In the Matter of Macklem,* 22 Fed. (2d) 426; 10 Am. B. R. (N. S.) 550, as set out on Pages 9, 10 and 11 of appellant's opening brief.

Appellees (appellees' brief, page 7) contend that a creditor receiving a preference seeks no advantage when he joins with other petitioning creditors to have the property of the alleged bankrupt subjected to the jurisdiction of the bankruptcy court and that it makes no material difference whether the petitioning creditor, who has received

a voidable preference, surrenders his preference prior to being counted as a petitioning creditor. This is obviously not the situation. One of the many evils which the Chandler Act and the decisions existing prior to its enactment is intended to remedy was the refusal of a creditor holding a voidable preference to surrender or offer to surrender said preference in the petition. The preferred creditor might, if not compelled to so surrender his preference in the petition, refuse to do so later during the administration of the estate and thereby subject the trustee and the estate to the financial burden and effort of prosecuting the proceedings to set aside the preference. Hence, the question as to whether a petitioning creditor has received a voidable preference is an issue in a proceeding had under an involuntary petition in bankruptcy. It is therefore submitted that the District Court refusal herein to consider whether the appellees had received preferences was clearly error.

Respectfully submitted,

Moe M. Tonkon,

Attorney for Appellant.

No. 9824

United States

Circuit Court of Appeals

For the Ninth Circuit.

ARTESIAN WATER COMPANY, a corporation,
Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

Transcript of the Record

Upon Petition to Review a Decision of the United States Board of Tax Appeals.

PARKER PRINTING COMPANY, 545 SANSOME STREET, SAN FRANCISCO

No. 9824

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[Clerk's Note: When deemed likely to be of an important nature, errors or doubtful matters appearing in the original certified record are printed literally in italic; and, likewise, cancelled matter appearing in the original certified record is printed and cancelled herein accordingly. When possible, an omission from the text is indicated by printing in italic the two words between which the omission seems to occur.]

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APPEARANCES:

For Taxpayer:
GEORGE A. WITTER, Esq.

For Comm'r:
E. A. TONJES, Esq.

Docket No. 100842

ARTESIAN WATER COMPANY,
Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

DOCKET ENTRIES

1939

Dec. 12—Petition received and filed. Taxpayer notified. (Fee paid).

Dec. 12—Copy of petition served on General Counsel.

1940

Jan. 23—Answer filed by General Counsel.

Jan. 23—Request for circuit hearing Los Angeles, Calif., filed by General Counsel.

Jan. 25—Notice issued placing proceeding on Los Angeles, Calendar. Answer and request served.

Apr. 5—Motion to place on Circuit Calendar for hearing in Los Angeles, California in June, 1940, filed by taxpayer.

1940

Apr. 11—Hearing set June 3, 1940, in Los Angeles, California.

June 11—Hearing had before Mr. Black on merits. Submitted. Amended petition and answer to amend petition filed. Copies served. Petitioner's brief due July 26, 1940. Respondent's Aug. 26, 1940. Reply Sept. 10, 1940.

July 11—Transcript of hearing of June 11, 1940, filed.

July 22—Brief filed by taxpayer. 7/22/40 copy served on General Counsel.

Aug. 26—Brief filed by General Counsel.

Sept. 5—Motion for extension of 20 days to file reply brief filed by taxpayer. 9/5/40 granted.

Sept. 20—Reply brief filed by taxpayer. 9/20/40 copy served on General Counsel.

1941

Jan. 22—Findings of fact and opinion rendered, Mr. Black, Div. 15. Decision will be entered for the respondent.

Jan. 24—Decision entered, Black, Div. 15.

Apr. 16—Petition for review by United States Circuit Court of Appeals, Ninth Circuit, filed by taxpayer.

Apr. 16—Praecipe filed by taxpayer.

Apr. 17—Proof of service of petition for review filed by taxpayer.

Apr. 17—Proof of service of praecipe filed. [1*]

*Page numbering appearing at foot of page of original certified Transcript of Record.

United States Board of Tax Appeals

Docket No. 100824

ARTESIAN WATER COMPANY,

Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,

Respondent.

PETITION

The above named Petitioner hereby appeals from the determination of the Respondent set forth in his deficiency letter dated September 21, 1939, symbols IT:LA FHG-90D, and as a basis of this proceeding alleges as follows:

I.

Petitioner is a corporation organized and existing under and by virtue of the laws of the State of California with its principal place of business at Los Angeles, California.

II.

The deficiency letter, copy of which is attached hereto and marked Exhibit "A", was mailed to the Petitioner on or about September 21, 1939.

III.

The taxes in controversy are for the calendar year 1937 and amount to the sum of $7,380.33.

IV.

The determination of taxes set forth in said deficiency letter is based upon the following error:

Respondent erred in imposing a surtax upon the undistributed profits of the Petitioner. [2]

V.

The facts upon which Petitioner relies as a basis for this proceeding are as follows:

The Petitioner was placed in receivership under jurisdiction of the Superior Court of the State of California in and for Los Angeles County in the year 1935 and remained continuously in receivership until finally discharged February 8, 1939. During the entire year 1937 Petitioner was in State Receivership and insolvent.

In 1929 and 1930 the Petitioner borrowed from the Pacific Mutual Life Insurance Company of California a total amount of $210,000.00, evidenced by four notes, all of which matured on November 12, 1934. These notes were secured by a mortgage on the lands owned by the Petitioner. The Petitioner was unable to make payment on the notes and on November 7, 1934, made application for a renewal or extension. This request was rejected by letter dated November 9, 1934, but time for the payment of the loan was thereafter advanced from quarter to quarter during the year 1935 and the early part of 1936.

In 1936 the Insurance Commissioner of the State of California made a special investigation of the

Pacific Mutual Life Insurance Company of California, as a result of which he severely criticized the loans to this Petitioner. The Commissioner appointed a Conservator for the Insurance Company. The Conservator of the Company made repeated and insistent demands upon the Petitioner, then in receivership, for payment of its loans. The Petitioner was wholly unable to meet such demands. The Petitioner, acting through [3] its Receiver, made efforts to refinance the loan or a portion thereof but without success. On or about September 1, 1936, the Receiver of the Petitioner began making monthly payments to the Conservator. During the year 1937 the Petitioner paid said Conservator the amount of interest due on said notes and approximately $83,000.00 on principal. On December 31, 1937, the balance owing to said Conservator was $100,250.00 on account of said notes. The Petitioner's net taxable income for 1937 was $54,101.14. During all of the year 1937 the lands and leasehold of the Petitioner were assigned to the said insurance company as security for said loans and said leasehold represented 97% of the Petitioner's income .

Wherefore, Petitioner prays that the Board hear and determine this appeal and render judgment in accordance with the foregoing.

GEORGE G. WITTER (Sgd)
Attorney for Petitioner
453 South Spring Street
Los Angeles, California [4]

State of California,
County of Los Angeles—ss.

Howard C. Bonsall, being duly sworn, deposes and says: That he is the President of the Artesian Water Company, the Petitioner named in the foregoing petition, that he is duly authorized to verify the same; that he has read the said petition and is familiar with the statements contained therein and that the facts stated are true as he verily believes.

HOWARD C. BONSALL (Sgd)

Subscribed and sworn to before me this 6th day of December, 1939.

[Seal] ROLAND FRIESS (Sgd)
Notary Public in and for said County and State.

My Com. expires Nov. 25, 1942. [5]

EXHIBIT "A"

Treasury Department
Internal Revenue Service
12th Floor
U. S. Post Office and Court House
Los Angeles, California

Sep. 21, 1939

Office of
Internal Revenue
Agent in Charge
Los Angeles Division
IT:LA
FHG-90D
Artesian Water Company,
Consolidated Building,
Sixth and Hill Streets,
Los Angeles, California.

Sirs:

You are advised that the determination of your income tax liability for the taxable year 1937 discloses a deficiency of $7,380.33 as shown in the statement attached.

In accordance with the provisions of existing internal revenue laws, notice is hereby given of the deficiency mentioned.

Within 90 days (not counting Sunday or a legal holiday in the District of Columbia as the 90th day) from the date of the mailing of this letter, you may file a petition with the United States Board of Tax Appeals for a redetermination of the deficiency.

Should you not desire to file a petition, you are requested to execute the enclosed form and forward it to Internal Revenue Agent in Charge, Los Angeles, California, for the attention of IT:LA:FC. The signing and filing of this form will expedite the closing of your return by permitting an early assessment of the deficiency, and will prevent the accumulation of interest, since the interest period terminates 30 days after filing the form, or on the date assessment is made, whichever is earlier.

Respectfully,

GUY T. HELVERING,

Commissioner,

By (Signed) GEORGE D. MARTIN

Internal Revenue Agent in Charge.

Enclosures:

Statement.

Form of Waiver. [6]

FHG-MAH

STATEMENT

IT:LA
FHG-90D

Artesian Water Company,
Consolidated Building,
Sixth and Hill Streets,
Los Angeles, California.
Tax Liability for the Taxable Year Ended
December 31, 1937.

Income Tax Liability—$14,335.50
Assessed—$6,955.17
Deficiency—$7,380.33

In making this determination of your income tax liability, careful consideration has been given to the report of examination dated January 13, 1939; to the protest dated February 7, 1939; to the statements made at the conference held on February 28, 1939; and to Bureau letters dated March 3, 1939 and May 9, 1939.

While your corporation was in receivership during the entire taxable year, such receivership was terminated and the receiver discharged on February 23, 1939; and the assessment of income tax made under the provisions of Section 274 of the Revenue Act of 1936, of which you were advised in Bureau letter dated March 3, 1939, has been abated.

A copy of this letter and statement has been mailed to your representative, Mr. George G. Witter, Citizens National Bank Building, Los Angeles, California, in accordance with the authority contained

in the power of attorney executed by you and on file with the Bureau. [7]

Net Income

Taxable year ended December 31, 1937.

Net income as disclosed by return.....$54,101.14

No change is made in the net income as reported in the return filed for the taxable year, and the deficiency stated herein is due to the computation of the surtax on undistributed profits imposed by Section 14 of the Revenue Act of 1936, for which no computation was included in the return.

The contention made, in both the return and the protest, that the corporation was not liable in the taxable year for the surtax imposed by the said Section 14, is denied for the reason that the evidence presented fails to show that you came within the purview of the exemption granted by Section 14 (d)(2).

In computing the surtax only the amount of $8,250.00 paid on relevant indebtedness is allowed as a credit for contracts restricting dividend payments, under the provisions of Section 26(c)(1) of the Revenue Act of 1936, for the reason that the information presented fails to substantiate that a greater credit is allowable. [8]

COMPUTATION OF TAX

Taxable year ended December 31, 1937

NORMAL INCOME TAX

Taxable net income		$54,101.14
Less: Excess-profits tax		None
Normal—tax net income		$54,101.14
Normal tax:		
8% of $ 2,000.00	$ 160.00	
11% of 13,000.00	1,430.00	
13% of 25,000.00	3,250.00	
15% of 14,101.14	2,115.17	
Total normal tax	$6,955.17	

SURTAX ON UNDISTRIBUTED PROFITS

Taxable net income		$54,101.14
Less: Normal tax		6,955.17
Adjusted net income		$47,145.97
Less: Credit for contracts restricting dividend payments		8,250.00
Undistributed net income		$38,895.97
Surtax:		
7% of $ 5,000.00	$ 350.00	
12% of 4,714.60	565.75	
17% of 9,429.20	1,602.96	
22% of 9,429.19	2,074.42	
27% of 10,322.98	2,787.20	
Total surtax	$ 7,380.33	
Normal tax	6,955.17	
Total income tax (normal tax and surtax)		$14,335.50

Income tax assessed (normal tax and surtax):			
Original list, account No. 402482		$6,955.17	
Additional, page 0, line 0, Commissioner's #2 list, March 10, 1939 (Sec. 274)	$7,380.33		
Less: Abatement allowed July 28, 1939	7,380.33	0.00	
Net amount assessed			6,955.17
Deficiency of income tax			$ 7,380.33

[Endorsed]: U. S. B. T. A. Filed Dec. 12, 1939.

[9]

[Title of Board and Cause.]

ANSWER

The Commissioner of Internal Revenue, by his attorney, J. P. Wenchel, Chief Counsel, Bureau of Internal Revenue, for answer to the petition of the above-named taxpayer, admits and denies as follows:

I and II. Admits the allegations contained in paragraphs I and II of the petition.

III. Admits that the taxes in controversy are for the calendar year 1937; denies the remainder of the allegations contained in paragraph III of the petition.

IV. Denies the allegations of error contained in paragraph IV of the petition.

V. Denies the allegations of fact contained in paragraph V of the petition.

VI. Denies each and every allegation contained in the petition not hereinbefore specifically admitted or denied [10]

Wherefore, it is prayed that the determination of the Commissioner be approved.

(Signed) J. P. WENCHEL
FTH
Chief Counsel,
Bureau of Internal Revenue

Of Counsel:
ALVA C. BAIRD,
FRANK T. HORNER,
E. A. TONJES,
Special Attorneys,
Bureau of Internal Revenue.

EAT/mm 1/15/40

[Endorsed]: U. S. B. T. A. Filed Jan. 23, 1940. [11]

[Title of Board and Cause.]

AMENDED PETITION

The above named Petitioner hereby appeals from the determination of the Respondent set forth in his deficiency letter dated September 21, 1939, symbols IT:LA FHG-90D, and as a basis of this proceeding alleges as follows:

I.

Petitioner is a corporation organized and existing under and by virtue of the laws of the State of California with its principal place of business at Los Angeles, California.

II.

The deficiency letter, copy of which is attached hereto and marked Exhibit "A", was mailed to the Petitioner on or about September 21, 1939.

III.

The taxes in controversy are for the calendar year 1937 and amount to the sum of $7,380.33.

IV.

The determination of taxes set forth in said deficiency letter is based upon the following error:

Respondent erred in imposing a surtax upon the undistributed profits of the Petitioner. [12]

V.

The facts upon which Petitioner relies as a basis for this proceeding are as follows:

The Petitioner was placed in receivership under jurisdiction of the Superior Court of the State of California in and for Los Angeles County in the year 1935 and remained continuously in receivership until finally discharged February 8, 1939. During the entire year 1937 Petitioner was in State Receivership and insolvent.

In 1929 and 1930 the Petitioner borrowed from the Pacific Mutual Life Insurance Company of

California a total amount of $210,000.00, evidenced by four notes, all of which matured on November 12, 1934. These notes were secured by a mortgage on the lands owned by the Petitioner. The Petitioner was unable to make payment on the notes and on November 7, 1934, made application for a renewal or extension. This request was rejected by letter dated November 9, 1934, but time for the payment of the loan was thereafter advanced from quarter to quarter during the year 1935 and the early part of 1936.

In 1936 the Insurance Commissioner of the State of California made a special investigation of the Pacific Mutual Life Insurance Company of California, as a result of which he severely criticized the loans to this Petitioner. The Commissioner appointed a Conservator for the Insurance Company. The Conservator of the Company made repeated and insistent demands upon the Petitioner, then in receivership, for payment of its loans. The Petitioner was wholly unable to meet such demands. The Petitioner, acting through its Receiver, made efforts to refinance the loan or a [13] portion thereof but without success. On or about September 1, 1936, the Receiver of the Petitioner began making monthly payments to the Conservator. During the year 1937 the Petitioner paid said Conservator the amount of interest due on said notes and approximately $83,000.00 on principal. On December 31, 1937, the balance owing to said Conservator was $100,250.00 on account of said notes. The Petition-

er's net taxable income for 1937 was $54,101.14. During all of the year 1937 the lands and leasehold of the Petitioner were assigned to the said insurance company as security for said loans and said leasehold represented 97% of the Petitioner's income.

On January 1, 1937, the Petitioner, then in receivership still, owed on account of notes which had matured more than two years before, the principal sum of $183,250.00. It had an operating deficit on January 1, 1937, of $50,571.97. On December 31, 1937, it still owed on account of said notes the principal sum of $100,250.00 and had an earned surplus of $34,442.50. Said deficit and earned surplus as stated, however, was determined without any deduction for depletion. If depletion were applied, there would still be a deficit at the close of the year 1937.

The following quoted sections are taken from the Civil Code of the State of California, and were in full force and effect during all the period mentioned in this petition.

> "§346. Cash or Property Dividends. A corporation may declare dividends payable in cash or in property only as follows:
>
> "(1) Out of earned surplus; or
>
> "(2) Despite the fact that the net assets of the corporation amount to less than the stated capital, [14] out of net profits earned during the preceding accounting period which shall not be less than six months nor more than one year in duration; or
>
> * * * * * * *

"Dividends: No dividends shall be declared when there is reasonable ground for believing that thereupon the corporation's debts and liabilities would exceed its assets or that it would be unable to meet its debts and liabilities as they mature.

* * * * * * *

"Wasting Asset Corporation. A wasting asset corporation, that is a corporation engaged solely or substantially in the exploitation of mines, oil wells, gas wells, patents or other wasting assets, or organized solely or substantially to liquidate specific assets, may distribute the net income derived from the exploitation of such wasting assets or the net proceeds derived from such liquidation without making any deduction or allowance for the depletion of such assets incidental to the lapse of time, consumption, liquidation or exploitation; subject, however, to adequate provision for meeting debts and liabilities and the liquidation preferences of outstanding shares and to notice to shareholders that no deduction or allowance has been made for such depletion. (Added by Stats. 1931, p. 1803; Amended by Stats. 1933, p. 1384.)

* * * * * * *

"§363. Unlawful Dividends, Purchases and Distribution. Except as provided in this title, the directors of a corporation shall not authorize or ratify the purchase by it of its shares or declare or pay dividends or authorize or ratify

the withdrawal or distribution of any part of its assets among its shareholders."

Said Petitioner was wholly unable to make adequate provision for payment of its indebtedness in the year 1937. Its net taxable income was $54,101.14. It actually paid $83,000.00 on its indebtedness in 1937. It still owed $100,250.00 at the end of the year 1937, which indebtedness at that time was over three years in default and bearing interest at the rate of [15] Seven Per Cent. Had the Petitioner applied its total gross receipts to payment of said indebtedness in 1937 it still would not have made adequate provision for payment of indebtedness.

Said Petitioner was prohibited under said laws from declaring any dividends during 1937. Said laws are a part of the Petitioner's charter and constituted a contract restricting the declaration of any dividends during 1937.

To secure said notes the Petitioner had assigned in writing all rents and royalties from its lands to the owner and holder of said notes and said assignment constituted a contract restricting its declaration of dividends throughout the year 1937.

Wherefore, Petitioner prays that the Board hear and determine this appeal and render judgment in accordance with the foregoing.

GEORGE G. WITTER (Sgd)
Attorney for Petitioner
453 South Spring Street
Los Angeles, California.

[16]

State of California,
County of Los Angeles—ss.

Howard C. Bonsall, being duly sworn, deposes and says: That he is the President of the Artesian Water Company, the Petitioner named in the foregoing Amended Petition, that he is duly authorized to verify the same; that he has read the said Amended Petition and is familiar with the statements contained therein and that the facts stated are true as he verily believes.

HOWARD C. BONSALL (Sgd)

Subscribed and sworn to before me this 4th day of June, 1940.

[Seal] ROLAND FRIESS (Sgd)
Notary Public in and for said County and State.

For Exhibit "A" see Exhibit "A" attached to petition.

[Endorsed]: U.S.B.T.A. Filed at hearing Jun. 11, 1940. [17]

[Title of Board and Cause.]

ANSWER TO AMENDED PETITION

The Commissioner of Internal Revenue, by his attorney, J. P. Wenchel, Chief Counsel, Bureau of Internal Revenue, for answer to the amended petition of the above-named taxpayer, admits and denies as follows:

I and II. Admits the allegations contained in paragraphs I and II of the amended petition.

III. Admits that the taxes in controversy are for the calendar year 1937; denies the remainder of the allegations contained in paragraph III of the amended petition.

IV. Denies the allegations of error contained in paragraph IV of the amended petition.

V. Denies the allegations of fact contained in paragraph V of the amended petition.

VI. Denies each and every allegation contained in the amended petition not hereinbefore specifically admitted or denied. [18]

Wherefore, it is prayed that the determination of the Commissioner be approved.

J. P. WENCHEL,
Chief Counsel,
Bureau of Internal Revenue.

Of Counsel:

ALVA C. BAIRD,
FRANK T. HORNER,
E. A. TONJES,
Special Attorneys,
Bureau of Internal Revenue.

EAT/mm 6/4/40.

[Endorsed]: U.S.B.T.A. Filed Jun. 11, 1940. [19]

[Title of Board and Cause.]

Docket No. 100824. Promulgated January 22, 1941.

1. Petitioner during the taxable year was in the hands of a receiver but was not insolvent. The receivership had not been instituted by the corporation's creditors but by a dissatisfied stockholder. Petitioner had assets which considerably exceeded its liabilities and during the taxable year had a net income of $54,101.14 and paid to its principal creditor very substantial payments on its indebtedness. Held, that petitioner is not exempt from the undistributed profits surtax as an insolvent corporation in receivership, under the provisions of section 14 (d) (2), Revenue Act of 1936.

2. Petitioner in the beginning of the taxable year had a deficit, but with its earnings, in the taxable year that deficit was wiped out and at the end of the year it had an earned surplus. Held, that the applicable code of California, which prevented petitioner from declaring any dividend so long as it had a deficit, is not a contract restricting the payment of dividends within the meaning of section 26 (c) (1), Revenue Act of 1936. Helvering v. Northwest Steel Rolling Mills, Inc., ... U. S. .....

3. Petitioner, to secure its indebtedness to an insurance company which was its principal creditor, several years prior to the taxable

year gave a mortgage on two farms which it owned, and as additional security it assigned certain oil royalties which it was to receive under the terms of an oil lease. These oil royalties were to be paid to petitioner and not to the creditor. Held, there is nothing shown in the assignments of these oil royalties as additional security which expressly restricted petitioner in the payment of dividends within the meaning of section 26 (c) (1), Revenue Act of 1936.

George G. Witter, Esq., for the petitioner.
E. A. Tonjes, Esq., for the respondent.

The Commissioner has determined a deficiency of $7,380.33 in petitioner's surtax liability for the year ended December 31, 1937. The Commissioner in his deficiency notice, in explanation of his determination of the deficiency, stated as follows:

> No change is made in the net income as reported in the return filed for the taxable year, and the deficiency stated herein is due to the computation of the surtax on undistributed profits imposed by Section 14 of the Revenue Act of 1936, for which no computation was included in the return.
>
> The contention made, in both the return and the protest, that the corporation was not liable in the taxable year for the surtax imposed by the said Section 14, [20] is denied for the reason that the evidence presented fails to show

that you came within the purview of the exemption granted by Section 14 (d) (2).

In computing the surtax only the amount of $8,250.00 paid on relevant indebtedness is allowed as a credit for contracts restricting dividend payments, under the provisions of Section 26 (c) (1) of the Revenue Act of 1936, for the reason that the information presented fails to substantiate that a greater credit is allowable.

To this action of the Commissioner imposing a surtax upon the undistributed profits of petitioner for the year 1937, the petitioner has assigned error. That assignment of error has been denied by the Commissioner and this presents the only issue for our decision.

FINDINGS OF FACT.

The petitioner is a California corporation, with principal place of business in the city of Los Angeles in said state.

Prior to and during the taxable year the petitioner owned certain assets which are described in part only in our record. Specifically two parcels of farm lands are legally described in a mortgage dated November 12, 1929, which is in evidence. Certain other properties, namely, the Shell Oil lease, the Home Villa Tract (a subdivision), and the Asphalt Paving Co. lease are referred to by names only in the evidence. From the income producing standpoint the Shell Oil lease, which yielded

more than 90 percent of all of petitioner's income during the taxable year, was the most valuable of all of these properties.

On November 12, 1929, the petitioner refinanced a loan owing by it to the Pacific Mutual Life Insurance Co., a corporation, hereinafter called the insurance company, by delivering to the latter two promissory notes, for $175,000 and $35,000, respectively, due five years after date and bearing interest at the rate of 6 percent per annum. To secure payment of these notes the petitioner executed in favor of the insurance company the mortgage hereinbefore mentioned covering its two parcels of farm lands described therein. In connection with the loan of $175,000 the petitioner assigned a lease in which the Shell Oil Co. was lessee as a further security for the payment of the note. In accordance with the terms of the agreement the Shell Oil Co. continued to pay all royalties to the petitioner. This practice was continued through the entire year 1937. There is no evidence in the record indicating that there was any contract in writing wherein the petitioner agreed not to pay any dividends during the period it was obligated under the $175,000 loan.

In addition to the mortgage and assignments so executed to secure payment of the said notes, a separate agreement was made respecting the $35,000 note to the effect that the petitioner would refrain from declaring any dividends upon its capital stock

so long as said [21] note remained unpaid. The Commissioner has allowed a credit in computing petitioner's undistributed profits tax for the amount paid by petitioner on this $35,000 note during the year 1937.

On July 16, 1935, William E. Ware was appointed receiver for the petitioner. The appointment of Ware as receiver arose out of an action by one J. Baldwin against Frederick Ringe, who was a stockholder of the petitioner. Baldwin had a judgment against Ringe in an amount approximating $200,000, which apparently could not be satisfied. After considerable investigation Baldwin located a safe deposit box used by Ringe which contained some of the capital stock of the Artesian Water Co., the petitioner. The stock was acquired by Baldwin under a sheriff's sale and in due course application was made to have the stock thus acquired by Baldwin transferred to him on the corporate records. The corporate officers refused to transfer the stock to Baldwin, whereupon he petitioned the Superior Court for the appointment of a receiver, on the ground that the corporate officers were not functioning under the code, which action resulted in the appointment of Ware as receiver. The receivership proceeding was not brought, nor was it continued, by reason of the inability of the corporation to pay its debts. Petitioner had substantially no debts except the amounts which it owed to the Pacific Mutual Life Insurance Co. This latter company had no part in the appointment of

the receiver, nor did it at any time press for the continuance of the receivership. The following is the order entered by the court upon the appointment of the receiver:

> It is hereby ordered that until further order of this Court William E. Ware, is named and appointed receiver of the Artesian Water Company, a corporation.
>
> That the receiver has, under the control of this court, power to bring and defend actions in his own name as receiver; to take, manage, operate and keep possession of the property, both real and personal, and each and all of it; to receive rents; collect debts; to compound for and compromise the same; and, subject to order of Court, to make transfers. The receiver is authorized to take possession of all books, records, correspondence and accounts of the said Artesian Water Company.
>
> Said receiver, subject to the Order of this court, shall have the full power and authority to operate the business of the Artesian Water Company in each and all of its departments, and in its entirety.

The receiver took over petitioner's properties on the above date and immediately began negotiations with the insurance company for an extension or renewal of the loans above described. While these negotiations were pending, a conservator was appointed for the insurance company by the State

Insurance Commissioner of California. There is nothing in the record to show that the appointment of the conservator by the insurance commissioner had anything to do with [22] the indebtedness of petitioner. After the conservator for the insurance company took charge, he disapproved said loans to petitioner on account of an interlocking relationship between the two corporations and refused any further extension of time for their payment. The receiver then attempted to refinance the loans through brokers but was unsuccessful owing to questions raised over his legal authority to pledge the intrusted assets.

In the situation, the insurance company consented to "informally" allow the petitioner until March 2, 1937, to refinance the loans, conditioned upon certain payments being made during the ensuing period. The petitioner paid $25,000 upon the notes during the year 1936 and made additional payments during 1937 which reduced the joint balance on the notes to $100,250. The petitioner owed no debts, other than current obligations, which were paid when due, at any time here shown, except its said debts to the insurance company, and was at all times here material a solvent corporation.

OPINION.

Black: The petitioner in its return for the taxable year reported gross income of $171,493.42, from which it claimed deductions amounting to $119,805.17, leaving a taxable net income of $54,101.14,

upon which it paid the normal income tax for the year.

The petitioner paid no surtax upon its undistributed profits for the year but in its return claimed an exemption from that obligation. It stated its claim for exemption as follows:

> Exemption from undistributed profits surtax is claimed on the following grounds: Attention is respectfully directed to Section 14 of the Revenue Act of 1936, part (d) (2) of which reads:
>
> (d) Exempt from surtax. The following corporations shall not be subject to the surtax imposed by this Section:
>
> (2) Domestic corporations which for any portion of the taxable year are in bankruptcy under the laws of the United States, or are insolvent and in receivership in any Court of the United States, or of any State, Territory, or the District of Columbia.
>
> The word "insolvent" was apparently used in its dual sense by Congress. The Senate Finance Committee Report on the Revenue Bill of 1936 of June 1, 1936, on page 15, in discussing Section 14 (d) (2), said:
>
> The Finance Committee Bill also avoids the possibility of tax avoidance by collusive receiverships by limiting the provision to cases in which the corporation is in bankruptcy under the Federal bankruptcy laws, and to cases in which it is insolvent, i. e., its lia-

> bilities are in excess of its assets or it is unable to pay the claims of creditors as they mature—and in receivership in Federal or State Courts.

The taxpayer was certainly unable to pay the claims of its creditors as they matured. That is, it was unable to pay them in the usual course of business out [23] of quick assets without selling its capital assets. 32 Corpus Juris 806 states that the word "insolvency" has two meanings:

> In its general and popular meaning, the term denotes the state of one whose entire property and assets, when converted into money without unreasonable haste or sacrifice, are insufficient to pay his debts: But it is frequently used in the more restricted sense to express the inability of a person to pay his debts as they become due in the ordinary course of business.

Creditors claims, referred to above, which the corporation was unable to pay at maturity, consist of balance due the Pacific Mutual Life Insurance Company on account of money borrowed on November 12, 1929, and represented by two notes, one for $35,000 and one for $175,000. The note for $35,000 carried with it a specific agreement prohibiting the payment of dividends until said note was paid. During 1936 the sum of $26,750 was paid on this note leaving a balance of $8,250 which balance was paid

during 1937, whereupon the note and collateral agreement were cancelled.

Similarly, during 1937 payments totaling $74,750 were made on the note for $175,000, making a grand total of payments made of $83,000.

The corporation owns subdivision land and oil producing property. The oil land is under lease to Shell Oil Company. The corporation secured its note to the Pacific Mutual Life Insurance Company by a mortgage on its properties, and gave as collateral security an assignment of the oil lease "together with all rents due, or to become due thereunder." The mortgagee notified Shell Oil Co. of the pledge of the lease and rents and instructed Shell Oil Co. to continue to pay the rents and royalties due under the lease to the corporation until further notice. The note and mortgage became due November 30, 1934, and is still past due. It has not been extended or renewed, and will outlaw November 30, 1938.

The corporation has never been in a position to pay off the mortgage out of current assets. From the foregoing, it is apparent, therefore, the corporation was insolvent and in receivership during the taxable year 1937, and is exempt from the surtax under Section 14.

The respondent in his audit disallowed petitioner's claim for exemption as an insolvent corporation, but, in recognition of its agreement not to

declare dividends so long as the $35,000 note remained unpaid, allowed it a credit from the adjusted base in amount of $8,250, under authority of section 26 (c) (1) of the Revenue Act of 1936.[1]

Petitioner, in its brief, states that the points which it relies upon are as follows:

> 1. The petitioner was in receivership and insolvent in the taxable year.
>
> 2. The California codes prohibited the declaration of dividends by the petitioner during the taxable year. [24]

We shall take these points up in their order. As to point 1, it is clear that petitioner was in receivership, but it is also equally clear that this receivership was not occasioned by any insolvency of petitioner. It was due to an altogether different cause.

---

[1]Sec. 26. Credits of Corporations.

* * * * *

(c) Contracts Restricting Payment of Dividends.—

(1) Prohibition on Payment of Dividends.—An amount equal to the excess of the adjusted net income over the aggregate of the amounts which can be distributed within the taxable year as dividends without violating a provision of a written contract executed by the corporation prior to May 1, 1936, which provision expressly deals with the payment of dividends. If a corporation would be entitled to a credit under this paragraph because of a contract provision and also to one or more credits because of other contract provisions, only the largest of such credits shall be allowed, and for such purpose if two or more credits are equal in amount only one shall be taken into account.

Petitioner concedes that the receivership was not instituted by its creditor, the insurance company, nor was it prolonged by any insistence on the part of the insurance company. Petitioner does contend, however, that in the taxable year 1937 it was insolvent within the meaning of the applicable statute, and that, when the two conditions exist simultaneously, namely, insolvency and receivership, then the exemption provided by section 14 (d) (2) applies. Petitioner, in support of its contention that it was insolvent during the taxable year within the meaning of the act, quotes from Dutcher v. Wright, 94 U. S. 553:

> Insolvency, in the sense of the Bankrupt Act, means that the party whose business affairs are in question is unabe to pay his debts as they become due, in the ordinary course of his daily transactions; and a creditor may be said to have reasonable cause to believe his debtor to be insolvent when such a state of facts is brought to his notice respecting the affairs and pecuniary condition of his debtor as would lead a prudent man to the conclusion that the debtor is unable to meet his obligations as they mature, in the ordinary course of his business. Buchanan v. Smith, 16 Wal., 308, 21 L. Ed., 286; Toof v. Martin, 13 Wal. 1, 40, 20 L. Ed., 481. * * *

That the word "insolvent" as used in section 14 (d) (2) was intended by Congress to carry the meaning used in the above language by the Supreme

Court, petitioner contends is evidenced by Senate Finance Committee Report of June 1, 1936, on the Revenue Bill of 1936, where on page 15, in discussing section 14 (d) (2), it is said:

> The Finance Committee Bill also avoids the possibility of tax avoidance by collusive Receiverships by limiting the provision to cases in which the corporation is in bankruptcy under the Federal bankruptcy laws, and to cases in which it is insolvent, i. e., its liabilities are in excess of its assets or it is unable to pay the claims of creditors as they mature—and in receivership in Federal or State Courts.

We accept as correct the contention which petitioner makes as to the meaning of the word "insolvent" as used in section 14 (d) (2). We do not think, however, that the evidence shows that petitioner was "insolvent" within the meaning of the act and the foregoing definition at any time during the taxable year. In a balance sheet attached to its income tax return for the taxable year, its total assets are listed at a value of $1,162,789.84; its total liabilities, exclusive of capital stock and surplus, are listed at $144,255.21. It had net income in 1937 of $54,101.14.

While it did not finish paying all of its indebtedness to the insurance company in 1937, it paid $83,000 of it in that year and, as has already been stated, this creditor had nothing whatever to do with [25] instituting the receivership and took no

part in prolonging it. Under these circumstances we can not hold that petitioner was an insolvent corporation in receivership during the taxable year. It was not exempt under section 14 (d) (2). On this point we sustain respondent.

As to point 2, raised in petitioner's brief, it is equally clear that the respondent must prevail. The question of whether or not state laws and/or charter provisions of a corporation create contractual relations recognizable in determining Federal income tax questions has been the subject of diverse decisions in different courts, notably in Northwest Steel Rolling Mills, Inc. v. Commissioner, 110 Fed. (2d) 286, where the Circuit Court of Appeals for the Ninth Circuit sustained the position herein contended for by the petitioner; and in Crane Johnson Co. v. Commissioner, 105 Fed. (2d) 740, wherein the Circuit Court of Appeals for the Eighth Circuit held to the opposite view. To settle this conflict in Circuit Court opinions, the Supreme Court granted certiorari in both cases (309 U. S. 692; 311 U. S. —) and rendered its decision sustaining the Eighth Circuit Court's views in Crane Johnson Co. v. Commissioner, —— U. S. ——, and reversing the Ninth Circuit Court's decision in Helvering v. Northeast Steel Rolling Mills, Inc., —— U. S. —— (Nov. 12, 1940). Following the Supreme Court's decision in these two cases we sustain respondent as to point 2.

We have disposed of the two points raised by petitioner in its original brief. The petitioner, in its reply brief, has raised a third point which in sub-

stance is this: Petitioner had assigned prior to May 1, 1936, as additional security for the payment of its $175,000 note due the insurance company, the oil royalties which it was to receive from the Shell Oil Co., and while this assignment did not expressly limit petitioner in the payment of dividends so long as any of the $175,000 note remained unpaid, nevertheless there was an implied restriction on the payment of dividends imposed by the agreement, and petitioner is entitled thereby to a credit under section 26 (c) (1), supra.

There is nothing to show that the assignment of the Shell Co. oil royalties by petitioner to its creditor, the Pacific Mutual Insurance Co., as further security for the payment of its $175,000 note, in any manner expressly restricted petitioner in the payment of dividends. This assignment is not in evidence and we do not know what written provisions it contained, but the witness who testified in regard to it did not say that the assignment dealt "expressly with the payment of dividends." Petitioner does not so contend in its brief. It simply contends that because petitioner had assigned these oil royalties to its creditor, as additional security for the payment of its notes, it [26] was by necessary implication prohibited from the payment of any dividends during the effective period of the assignment. We think this contention must be denied. Cf. Belle-vue Manufacturing Co., 43 B. T. A. —— (Dec. 6, 1940).

Petitioner does not make any claim that it is en-

titled to a credit under the provisions of section 26 (c) (2). On account, however, of the close connection between paragraphs (1) and (2) of section 26 (c) of the Revenue Act of 1936, perhaps we should say a word as to the applicability of section 26 (c) (2) to the facts of the instant case. We have considered the evidence carefully and we find no contract in evidence which would seem to fall within the provisions of section 26 (c) (2).

Our decision in G. B. R. Oil Corporation, 40 B. T. A. 738, which was under section 26 (c) (2), is not applicable to the facts in the instant case. In that case the taxpayer, to secure the loans with which to purchase certain oil leases and oil royalties, executed and delivered to the bank from which it was borrowing the money appropriate deeds of trust and also by separate instruments in writing assigned its interests in the properties to the bank in trust and authorized the bank to receive and collect all sums of money derived from the properties and to apply same on its indebtedness to the bank. Under those circumstances, we held that the taxpayer in computing its adjusted net income was entitled to a credit under section 26 (c) (2) of the amount paid on its indebtedness during the taxable year in compliance with the contract.

In the instant case, there was no requirement that the oil royalties received from the Shell Co. should be paid to petitioner's creditor, the insurance company, as there was in G. B. R. Oil Corporation, supra. On the contrary, the oil royalties were

to be paid to petitioner and were in fact paid to it. The insurance company had a mortgage on these oil royalty receipts, it is true, and it is undoubtedly true that a considerable portion of them was used as payments on petitioner's indebtedness to the insurance company, but it seems to us that this falls short of meeting the requirements of section 26 (c) (2). Cf. Nocona Cotton Seed Oil Co., 42 B. T. A. 1172.

For reasons above stated we think the facts in the instant case are distinguishable from those which were present in G. B. R. Oil Corporation, supra.

Decision will be entered for respondent. [27]

United States Board of Tax Appeals
Washington

Docket No. 100824

ARTESIAN WATER COMPANY,
Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

DECISION

Pursuant to the determination of the Board, as set forth in its Findings of Fact and Opinion, promulgated January 22, 1941, it is

Ordered and decided: That there is a deficiency of $7,380.33 in surtax liability for the year 1937.

Enter:

Entered Jan. 24, 1941.

[Seal] (Signed) EUGENE BLACK
Member [28]

In the United States Circuit Court of Appeals for the Ninth Circuit

[Title of Cause.]

PETITION FOR REVIEW

To the Honorable the Judges of the United States Circuit Court of Appeals for the Ninth Circuit:

Artesian Water Company, a California corporation, with its principal place of business at Los Angeles, California, in support of its petition filed in pursuance of the provisions of Section 1001 of the Revenue Act of 1926, for the review of the decision of the United States Board of Tax Appeals rendered on January 22, 1941, approving a deficiency in income and undistributed profits taxes of the Artesian Water Company for the year ended December 31, 1937, in the sum of $7,380.33, respectfully shows to this Honorable Court as follows:

I.

Statement of the Nature of the Controversy.

Under date of September 21, 1939, the Commissioner of Internal Revenue mailed to the petitioner a final notice of deficiency in surtax on undistributed profits for the year 1937 [29] in the amount of $7380.33. Within 90 days from the date of said letter the petitioner filed its appeal with the United States Board of Tax Appeals. On the 11th day of June, 1940, a hearing of said appeal was had before a member of the United States Board of Tax Appeals, sitting at Los Angeles. Oral testimony was taken and recorded and documentary evidence introduced. On the 22nd day of January, 1941, the Board handed down its final decision denying the petitioner's contentions.

The petitioner filed its original income tax return for the year 1937, disclosing thereon net income for the year in the amount of $54,101.14 and an income tax thereon of $6,955.17, which it paid. When the Commissioner of Internal Revenue audited this return, he determined the net income reported thereon correct and the income tax shown thereon correct, but, further finding that the Company had not distributed this income to its stockholders as dividends, the Commissioner imposed a surtax on undistributed profits based on the rates found in Section 14 of the Revenue Act of 1936. The entire deficiency asserted consists of surtax on undistributed profits and not of income tax.

The taxpayer contended before the Board and now contends that it was not and is not subject to surtax for not distributing its net earnings in the year 1937 for the following reasons.

1. It was in receivership during the entire taxable year 1937 and was unable by any means within its power to pay its debts as they matured and therefore was exempt from such surtax [30] under Section 14(d)(2) of the Revenue Act of 1936.

2. The petitioner had mortgaged all of its income-producing assets to secure indebtedness which it owed and further had assigned its leases and its income to its creditors to secure such indebtedness. Such mortgage and assignment constituted a contract restricting it from the payment of dividends and therefore exempting it from surtax on undistributed profits under Section 26(c) of the Revenue Act of 1936.

3. In the year 1937, the petitioner was unable to pay its debts as they matured and was therefore prohibited under the Statutes of the State of California from the declaration of a dividend, and such statutes constituted a part of its charter and a contract restricting it from the declaration of dividends and rendering it exempt from the surtax on undistributed profits under the provisions of Section 26 of the Revenue Act of 1926.

II.

Designation of Court of Review.

The petitioner being aggrieved by the said decision of the Board of Tax Appeals and having at all

times had its principal place of business in the City of Los Angeles, State of California, and having filed its income tax return for the calendar year 1937 with the Collector of Internal Revenue for the Sixth District of California, desires a review of said decision by the United States Circuit Court of Appeals for the Ninth Circuit. [31]

Wherefore, your petitioner prays that this Honorable Court may review said decision and reverse and set aside the same.

ARTESIAN WATER COMPANY,
a Corporation.
By MARVIN OSBURN,
Assistant Secretary.
GEORGE G. WITTER,
Attorney for Petitioner.

[Endorsed]: U. S. B. T. A. Filed April 16, 1941. [32]

In the United States Circuit Court of Appeals
for the Ninth Circuit

[Title of Cause.]

NOTICE

To the General Counsel, Bureau of Internal Revenue, Attorney for for Respondent:

You are hereby notified that on the 16 day of April, 1941, a Petition for Review of the decision of the United States Board of Tax Appeals in the above-entitled cause was filed with the Clerk of the

Board, and a true copy of said Petition is herewith served upon you.

(s) GEORGE G. WITTER
Attorney for Petitioner

Receipt of a true copy of Petition for Review so filed is acknowledged this 17th day of April, 1941.

J. P. WENCHEL,
Chief Counsel,
Bureau of Internal Revenue,
Attorney for Respondent.

[Endorsed]: U. S. B. T. A. Filed Apr. 17, 1941.

[33]

Official Report of Proceedings

before the

U. S. Board of Tax Appeals

Docket No. 100842

ARTESIAN WATER COMPANY,
Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

Hearing at Los Angeles, California

Date June 11, 1940

Pages 1-40

[34]

[Title of Board and Cause.]

REPORTER'S MINUTES

Hearing at Los Angeles on the 11th day of June, 1940, at 10:15 o'clock, A. M.

The above-entitled proceeding came on for hearing on this the 11th day of June, 1940, before the Honorable Eugene Black, Member of the United States Board of Tax Appeals, at Los Angeles, California, pursuant to notice of hearing heretofore given; whereupon, the following proceedings were had and testimony heard, to-wit:

Appearances:

George G. Witter, Esq., (453 South Spring Street, Los Angeles, California), appearing on behalf of Petitioner.

E. A. Tonjes, Esq., (Honorable J. P. Wenchel, Chief Counsel, Bureau of Internal Revenue), appearing on behalf of the Commissioner of Internal Revenue, Respondent. [36]

PROCEEDINGS

The Clerk: Docket No. 100842, Artesian Water Company.

Appearing for the petitioner, George G. Witter.

And your address, Mr. Witter?

Mr. Witter: 453 South Spring Street, Los Angeles, California.

The Clerk: Mr. E. A. Tonjes, for the respondent.

Mr. Tonjes: That is correct, Mr. Clerk.

Mr. Witter: May it please the Board, Your Honor made an order from the bench granting leave to file an amended petition.

Mr. Tonjes: Respondent of course has no objection to that, Your Honor.

Mr. Witter: At this time I would like to file an amended petition.

The Member: The amended petition will be received and filed.

Mr. Tonjes: At this time I would like to have the privilege of filing an answer to the amended petition.

The Member: The answer will be received and filed.

Does the petitioner have any statement to make with reference to the issues involved in this case? [37]

Statement of Case on Behalf of Petitioner:

By Mr. Witter:

Mr. Witter: I should like to make a brief statement of the issues involved. Also, a very brief digest of the brief that is going to be offered.

The year involved here is the year 1937. The company, the Artesian Water Company, was a company that was organized in California in 1900. It was the owner of lands. In the year 1935 it was thrown into receivership and remained in receivership until 1939. So that during the entire taxable year involved here in 1937 the petitioner was put into state receivership.

Now, the tax that has been imposed by the Government is a surtax on undistributed profits, the deficiency amounting to seven thousand three hundred eighty some odd dollars.

The facts giving rise to this issue are briefly as follows: In the year 1929 the Artesian Water Company owed the Pacific Mutual Company an indebtedness that had been incurred long prior thereto, which amounted to a balance of $175,000. A new note was given in 1929 for that $175,000. An additional note was given in 1931 for $35,000, making a total indebtedness of $210,000.

Both of these notes matured in 1934. Nothing was paid on these notes between the dates they were given and [38] the date in 1934. In 1934 the company requested the insurance company to extend the period for payment and the insurance company refused.

Then the notes ran on without any payment being made thereon, and in 1935 the Artesian Water Company was put into state receivership. It wasn't put into state receivership by the Pacific Mutual Company to whom these notes were owed. Pacific Mutual Company was secured on those notes by mortgages on practically all of the assets—I will say all of the assets of value which the Artesian Water Company owned.

The principal income of the Artesian Water Company constituted royalties from an oil lease, and to secure these notes the Artesian Water Company had not only given a mortgage on all of its land of

value, and the lands comprised all its assets, but it also assigned to the insurance company all of the rents and royalties from the lease.

In the year 1937, the taxable year, the receiver was confronted with this situation: He had been able to pay on the $210,000 indebtedness up to January 1st approximately $25,000. So that at the beginning of the taxable year there was due on these loans approximately $185,000.

In the middle of the year 1936 a conservator was appointed for the Pacific Mutual and very close scrutiny made of all of its accounts. These notes to the Artesian [39] Water Company came under close scrutiny and came in for very severe criticism. The conservator insisted upon a collection being made immediately. The receiver made very strenuous efforts to get extensions of time, and the best that he was able to obtain in the way of an extension was to March 3, 1937, the insurance company calling for certain payments to be made each month, and the full balance to be paid under all circumstances by March 3, 1937.

The receiver was unable to make any payment of these notes in full or to liquidate either on March 3, 1937 or at any time during 1937. The receiver did what he could in making payments out of whatever income was received and reducing the notes. The Pacific Mutual made no further extension beyond March 3, 1937, but did not bring foreclosure suit.

Eventually, the notes were paid. The receivership

continued until 1939, and then the company emerged from the state receivership.

It is the contention of the taxpayer that it is not subject to undistributed profits tax because it was in state receivership and it was insolvent in the year 1937.

It is further the contention that under the California Codes it had no right to declare any dividends and the directors would have rendered themselves liable if they had done so, and that that would constitute an express [40] contract restricting the payment of dividends.

It is also contended that the assignment of all of the rents and royalties in writing to the note-holding creditor constituted a contract restricting the payment of dividends.

It is also contended that the statutes of this state pertaining to receivership constituted a contract which prevented this company from declaring any dividend during the year 1937.

The Member: All right, Mr. Witter.

Mr. Tonjes, do you have a statement you wish to make?

Statement of Case on Behalf of Respondent:

By Mr. Tonjes:

Mr. Tonjes: Yes.

If Your Honor please, respondent's position is that not only does the statute require that a corporation in order to be exempt from the surtax in question, be exempted, that it must be in receiver-

ship and insolvent, and it is the respondent's contention that the corporation was not insolvent.

That in so far as any restriction is contained in the law of the state of California with respect to the times or the circumstances under which a corporation can make distributions of dividends, do not constitute such a [41] contract in writing as required by the statute in order to be entitled to a dividend paid credit.

The Member: Very well.

We will receive the evidence now, Mr. Witter.

Mr. Witter: I will call Mr. Ware.

Evidence on Behalf of Petitioner:

Thereupon, the petitioner, to maintain the averments of its petition, introduced the following proof:

The Clerk: Give your name to the reporter, please.

Mr. Ware: William E. Ware.

MR. WILLIAM E. WARE,

called as a witness by and on behalf of the petitioner, having been first duly sworn, was examined and testified as follows:

Direct Examination

By Mr. Witter:

Q. Where do you live, Mr. Ware?

A. 174 Westgate Avenue, Brentwood Heights, Los Angeles.

Q. And how long have you lived in Los Angeles?

(Testimony of Mr. William E. Ware.)

A. Oh, thirty years.

Q. And what is your business?

A. Certified Public Accountant.

Q. Were you the receiver for the Artesian Water Company, this taxpayer? [42]

A. I was.

Q. How long were you receiver for that company?

A. From July 16, 1935 to February 8, 1939.

Q. And are you generally familiar with the history of that company? A. I am.

Q. Was the company organized in the state of California? A. It was.

Q. And did it always operate in the state of California? A. It did.

Q. What was the general nature of the assets of the company?

A. It consisted principally of real properties, some vacant acreage with oil leases, and some subdivision properties and vacant properties.

Q. Are you familiar with two notes that were outstanding at the time that you were appointed receiver for the Artesian Water Company?

A. Yes.

Mr. Witter: I will ask you, Mr. Clerk, to mark these documents for identification.

The Clerk: They will be marked Petitioner's Exhibits 1, 2, and 3 for identification. [43]

(The said documents so offered were marked Petitioner's Exhibits 1, 2, and 3, for identification.)

(Testimony of Mr. William E. Ware.)

By Mr. Witter:

Q. I hand you what has been marked Petitioner's Exhibit No. 3 and ask you to state what it is.

A. That is a certified copy of the order appointing the receiver, dated July 16, 1935.

Mr. Witter: I offer Petitioner's Exhibit No. 3 in evidence.

Mr. Tonjes: No objection.

The Member: Very well, it will be received as Petitioner's Exhibit No. 3.

(The said document so offered and received in evidence, was marked Petitioner's Exhibit 3, and made a part of this record.)

PETITIONER'S EXHIBIT NO. 3

In the Superior Court of the State of California in and for the County of Los Angeles.

No. 390338

J. C. BALDWIN,

Plaintiff,

vs.

FREDERICK H. RINDGE, MAY K. RINDGE, RHODA ADAMSON, MARVIN OSBURN, EDWARD L. STAEBLER, A. S. COOPER, HELEN N. RINDGE, P. B. GOWAN, S. N. WEST, GEORGE F. ARNOLD, M. F. PETERSON, RINDGE COMPANY, a corpora-

(Testimony of Mr. William E. Ware.)

tion, ARTESIAN WATER COMPANY, a corporation, JOHN DOE ONE, JOHN DOE TWO, JOHN DOE THREE, JOHN DOE FOUR, JANE ROE ONE, JANE ROE TWO, JOHN DOE ONE COMPANY, a corporation, JOHN DOE TWO COMPANY, a corporation, JOHN DOE THREE COMPANY, a corporation, and JOHN DOE AND RICHARD ROE, a co-partnership,

Defendant.

ORDER APPOINTING A RECEIVER.

Upon reading and filing the verified complaint of the plaintiff in the above entitled action, and upon the other papers on file herein, and good cause appearing therefor,—

It Is Hereby Ordered that until further order of this Court William E. Ware, is named and appointed receiver of the Artesian Water Company, a corporation.

That the receiver has, under the control of this court, power to bring and defend actions in his own name as receiver; to take, manage, operate, and keep possession of the property, both real and personal, and each and all of it; to receive rents, collect debts; to compound for and compromise the same; and, subject to order of Court, to make transfers. The receiver is authorized to take possession of all books, records, correspond-

(Testimony of Mr. William E. Ware.)

ence and accounts of the said Artesian Water Company.

Said receiver, subject to the Order of this court, shall have the full power and authority to operate the business of the Artesian Water Company in each and all of its departments, and in its entirety.

[82]

It Is Further Ordered that the defendants, and each and all of them, be and appear in Department 34 of the above entitled Superior Court on the 26th day of July, 1935, at 10 o'clock A. M., to show cause, if any they have, why the appointment of the Receiver herein should not be confirmed.

It Is Hereby Ordered that the plaintiff file an undertaking with sufficient sureties, in the amount of $1,000.00, conditioned according to law, and the Court does hereby state that said bond so required has been approved by this Court, and filed.

Be It Hereby Further Ordered that the Receiver give and file a bond, on qualifying, with sufficient sureties, in the sum of $2,000.00, conditioned according to law, and that the said Receiver take the oath required by law. The Court does hereby state that said bond has been furnished by the Receiver, has been approved by this Court, and filed, and, further, that said Receiver has now taken the said oath, as required by law, and as above provided for.

It Is Further Ordered that the said Receiver shall, within ten days after the date of this Order, file with the Court an inventory containing a com-

(Testimony of Mr. William E. Ware.)

plete and detailed list of all property of which he shall take possession by virtue of his appointment, and if he shall thereafter take possession of other property, he shall at once file a supplementary inventory thereof.

Dated: This 16th day of July, 1935.

WILSON
Judge of the Superior Court of Los Angeles County.

The foregoing instrument is a correct copy of the original on file and/or of record in this office. (Omitting Points and Authorities) KR

Attest July 16, 1935.

L. E. LAMPTON,
County Clerk and Clerk of the Superior Court of the State of California, in and for the County of Los Angeles.

By K. RANDALL
Deputy

[Endorsed]: Filed Jul 16 1935. L. E. Lampton, County Clerk, By J. E. Shaw, Deputy.

[Endorsed]: Petitioner's Exhibit No. 3. Admitted in evidence June 11, 1940. [83]

(Testimony of Mr. William E. Ware.)

By Mr. Witter:

Q. I hand you what has been marked Petitioner's Exhibit No. 1 and ask you to state what that is.

A. This is a mortgage note for $175,000 due to the Pacific Mutual Life Insurance Company of California by the Artesian Water Company, due in five years, with interest at the rate of six per cent per annum.

Mr. Witter: I offer in evidence Petitioner's Exhibit No. 1. [44]

Mr. Tonjes: No objection.

The Member: It will be received as Petitioner's Exhibit No. 1.

(The said document so offered and received in evidence, was marked Petitioner's Exhibit 1, and made a part of this record.)

PETITIONER'S EXHIBIT NO. 1

No. 6509

$175,000.00

Los Angeles, California, November 12, 1929.

Five years after date, for value received Artesian Water Company, a California Corporation, promises to pay to The Pacific Mutual Life Insurance Company of California, or order, at its office in Los Angeles the sum of One Hundred Seventy-Five Thousand Dollars, with interest from date until paid, at the rate of Six (6) per cent. per annum, payable Quarterly; should the interest not be so paid, it shall become a part of the principal

(Testimony of Mr. William E. Ware.)

and thereafter bear like interest as the principal. Should default be made in the payment of any installment of principal or interest when due, then the whole sum of principal and interest shall become immediately due and payable at the option of the holder of this note. Principal and interest payable in lawful money of the United States. This note is secured by a mortgage upon real property of even date herewith.

[Seal] ARTESIAN WATER COMPANY

By M. K. RINDGE
President

By A. S. COOPER
Secretary

[Stamped] Paid 7-25-38 (D) Pacific Mutual Life Insurance Co. Mortgage Loan Dept.

[Cancelled 7/25/38 R. Nehl]. [76]

(Testimony of Mr. William E. Ware.)

2-11-30	Int. paid	$2,280.38	to 2-12-30
5-13-30	Int. paid	$2,625.00	to 5-13-30
8-12-30	Int. paid	$2,625.00	to 8-12-30
11-12-30	Int. paid	$2,625.00	to 11-12-30
2-16-31	Int. paid	$2,625.00	to 2-12-31
5-19-31	Int. paid	$2,625.00	to 5-12-31
8-12-31	Int. paid	$2,625.00	to 8-12-31
11-12-31	Int. paid	$2,625.00	to 11-12-31
2-13-32	Int. paid	$2,625.00	to 2-12-32
5-17-32	Int. paid	$2,625.00	to 5-12-32
8-16-32	Int. paid	$2,625.00	to 8-12-32
11-12-32	Int. paid	$2,625.	to 11-12-32
2-11-33	Int. paid	$2,625.	to 2-12-33
5-11-33	Int. paid	$2,625.	to 5-12-33
8-16-33	Int. paid	$2,625.	to 8-12-33
11-11-33	Int. paid	$2,625.	to 11-12-33
2-10-34	Int. paid	$2,625.	to 2-12-34
5-14-34	Int. paid	$2,625.00	to 5-12-34
8-10-34	Int. paid	$2,625.00	to 8-12-34
11- 8-34	Int. paid	$2,625.00	to 11-12-34
2-12-35	Int. paid	$2,625.00	to 2-12-35
5-13-35	Int. paid	$2,625.00	to 5-12-35
8-21-35	Int. paid	$2,625.00	to 8-12-35
11-13-35	Int. paid	$2,625.00	to 11-12-35
2-17-36	Int. paid	$2,625.00	to 2-12-36
5-12-36	Int. paid	$2,625.	to 5-12-36
8-18-36	Int. paid	$2,625.	to 8-12-36
11-13-36	Int. paid	$2,625.	to 11-12-36
2-12-37	Int. paid	$2,625.	to 2-12-37
5-12-37	Int. paid	$2,611.71	to 5-12-37
8-13-37	Int. paid	$2,293.30	to 8-12-37
11-12-37	Int. paid	$1,933.	to 11-12-37

4- 1-37	Paid a/c principal $ 2,750	Unpaid balance $172,250
5- 3-37	Paid a/c principal $ 2,750	Unpaid balance $169,500
6- 1-37	Paid a/c principal $ 2,750	Unpaid balance $166,750
6-14-37	Paid a/c principal $20,000	Unpaid balance $146,750
7- 1-37	Paid a/c principal $ 2,750	Unpaid balance $144,000

(Testimony of Mr. William E. Ware.)

8- 2-37 Paid a/c principal $ 2,750 Unpaid balance $141,250
8-23-37 Paid a/c principal $10,000 Unpaid balance $131,250
9- 1-37 Paid a/c principal $ 2,750 Unpaid balance $128,500
10- 4-37 Paid a/c principal $ 2,750 Unpaid balance $125,750
11- 3-37 Paid a/c principal $ 2,750 Unpaid balance $123,000

[77]

PAYMENTS

Date Paid M. D. Y.	Date Due M. D. Y.	Credited on Interest	Principal	Balance Principal Unpaid
12- 1-37	A/c		2,750	120,250
12-16-37	A/c		20,000	100,250
1- 3-38	A/c		2,750	97,500
2- 1-38	A/c		2,750	94,750
2-14-38	2-12-38	1,602.88		
2-23-38	A/c		30,000	64,750
3- 2-38	A/c		2,750	62,000
4- 4-38	A/c		2,750	59,250
4-29-38	A/c		25,000	34,250
5- 2-38	A/c		2,750	31,500
5-11-38	5-12-38	918		
6- 1-38	A/c		2,750	28,750
6-30-38	A/c		2,750	26,000
7-18-38	A/c		11,590	14,410
7-25-38	In full	333.51	14,410	0

[Endorsed]: Petitioner's Exhibit One. Admitted in evidence June 11, 1940. [79]

(Testimony of Mr. William E. Ware.)

By Mr. Witter:

Q. Mr. Ware, this note for $175,000, marked Petitioner's Exhibit 1, do you know the history of that up to the date that it was given?

A. I think so.

Q. State briefly what the history was.

A. This represents a mortgage note which was given on November 12, 1929, secured by two parcels in Los Angeles County, two parcels of real estate in Los Angeles County, described as Parcel No. 1, being three hundred thirty acres of farm land located between Culver City and Inglewood, which is unimproved; and Parcel 2 representing fifty acres of farm land on six-tenths of a mile east of Washington Street in Culver City, which is also unimproved. It is also secured by the assignment of four leases.

Q. Oil leases?

A. No, not all of them. Some of them are farming leases, and a lease to the Asphalt Paving Company which had a small portion of the land there on which they had a plant [45] located.

Q. Testifying further as to the history of the loan, does it represent refinancing of an earlier debt owed by the company?

A. It does, yes.

Q. Do you recall when the predecessor note was given that this replaced?

A. Well, it represents a series of refinancings. You are going back as far as 1934. But the prin-

(Testimony of Mr. William E. Ware.)

cipal refinancing was in 1924, on which this loan came in.

Q. Does this $175,000 note represent the unpaid balance of former indebtedness incurred by the Artesian Water Company? A. It does.

Q. I hand you what has been marked for identification Petitioner's Exhibit 2 and ask you to state what that is.

A. This represents a note for $35,000 dated December 18, 1931, due November 12, 1934, given by the Artesian Water Company to the Pacific Mutual Life Insurance Company of California, with interest at the rate of six per cent per annum.

Mr. Witter: I offer in evidence Petitioner's Exhibit No. 2.

Mr. Tonjes: No objection, Your Honor.

The Member: It will be received as Petitioner's [46] Exhibit No. 2.

(The said document so offered and received in evidence, was marked Petitioner's Exhibit 2, and made a part of this record.)

PETITIONER'S EXHIBIT NO. 2

No. 6509

$35,000.00

Los Angeles, California, December 18, 1931.

November 12, 1934 after date, for value received Artesian Water Company, a California corporation, promises to pay to The Pacific Mutual Life Insurance Company of California, or order, at its

(Testimony of Mr. William E. Ware.)

office in Los Angeles, the sum of Thirty Five Thousand Dollars, with interest from date until paid, at the rate of Six (6) per cent. per annum, payable February 12, 1932 and Quarterly Thereafter; should the interest not be so paid, it shall become a part of the principal and thereafter bear like interest as the principal. Should default be made in the payment of any installment of principal or interest when due, then the whole sum of principal and interest shall become immediately due and payable at the option of the holder of this note. Principal and interest payable in lawful money of the United States. This note is given for an additional loan as provided by the terms of that certain mortgage dated November 12, 1929, made by undersigned to said The Pacific Mutual Life Insurance Company of California, recorded in Book 9596 of Official Records at page 14, Records of Los Angeles County, State of California, and is secured by all the terms and conditions of said mortgage.

[Seal] ARTESIAN WATER COMPANY

By M. K. RINDGE,
President.

By A. S. COOPER,
Secretary.

Paid 3-3-37 [Stamped on face]

Cancelled 3-3-37 [80]

(Testimony of Mr. William E. Ware.)

2-13-32	Int. paid	$245.00	to	2-12-32
5-17-32	Int. paid	$525.	to	5-12-32
8-16-32	Int. paid	$525.	to	8-12-32
11-12-32	Int. paid	$525.	to	11-12-32
2-11-33	Int. paid	$525.	to	2-12-33
5-11-33	Int. paid	$525.	to	5-12-33
8-16-33	Int. paid	$525.	to	8-12-33
11-11-33	Int. paid	$525.	to	11-12-33
2-10-34	Int. paid	$525.	to	2-12-34
5-14-34	Int. paid	$525.	to	5-12-34
8-10-34	Int. paid	$525.	to	8-12-34
11- 8-34	Int. paid	$525.	to	11-12-34
2-12-35	Int. paid	$525.	to	2-12-35
5-13-35	Int. paid	$525.	to	5-12-35
8-21-35	Int. paid	$525.	to	8-12-35
11-13-35	Int. paid	$525.	to	11-12-35
2-17-36	Int. paid	$525.00	to	2-12-36
5-12-36	Int. paid	$525.	to	5-12-36
8-18-36	Int. paid	$525.	to	8-12-36
11-13-36	Int. paid	$497.	to	11-12-36
2-13-37	Int. paid	$110.92	to	2-12-37

11-12-36
As of

11- 5-36	Paid a/c principal $24,000	Unpaid balance	$11,000
12- 1-36	Paid a/c principal $2,750	Unpaid balance	$ 8,250
1- 5-37	Paid a/c principal $2,750	Unpaid balance	$ 5,500
2- 2-37	Paid a/c principal $2,750	Unpaid balance	$ 2,750
3- 3-37	Paid a/c principal $2,750	Unpaid balance	$ 0

[Endorsed]: Petitioner's Exhibit No. 2. Admitted in evidence. June 11, 1940. [81]

(Testimony of Mr. William E. Ware.)

Mr. Witter: I offer in evidence the mortgage that went to secure the two notes that have just been introduced in evidence.

Mr. Tonjes: No objection.

The Member: It will be received as Petitioner's Exhibit No. 4.

(The said document so offered and received in evidence, was marked Petitioner's Exhibit 4, and made a part of this record.)

PETITIONER'S EXHIBIT No. 4

No. 6509

MORTGAGE

Artesian Water Company

to

The Pacific Mutual Life Insurance Company of California

This Mortgage, Made the twelfth day of November, A. D. nineteen hundred and twenty-nine, by Artesian Water Company, a California Corporation having its principal place of business at Los Angeles, California, Mortgagor, to The Pacific Mutual Life Insurance Company of California, a corporation organized and existing under the laws of the State of California, Mortgagee.

Witnesseth: That the Mortgagor hereby mortgages to the Mortgagee the real property situate in

(Testimony of Mr. William E. Ware.)

the County of Los Angeles, State of California, and described as follows, to-wit:

Parcel #1:

That part of the Rancho Cienega O'Paso de la Tijera, lying partly within and partly without the City of Los Angeles, in the County of Los Angeles, State of California, described as follows:

Beginning at the Northwest corner of said Rancho, said point being Station 6 of the Patent Survey thereof; thence South two (2) degrees West along the West line of said Rancho one hundred thirty-two and forty-four hundredths (132.44) chains; thence South eighty-eight (88) degrees East twenty-seven and eighteen hundredths (27.18) chains to the Easterly line of the four hundred forty-four (444) acre tract allotted to Rita Botiller de Aguilar by final decree of partition of said Rancho, a certified copy of which is recorded in Book 27, Page 74 of Deeds; thence North two (2) degrees East along said Easterly line one hundred sixteen and twenty-eight hundredths (116.28) chains, more or less, to the Northerly line of said Rancho; thence North fifty-seven (57) degrees West along said Northerly line twenty-four and seventy-five hundredths (24.75) chains to Station 4; thence North sixty-five (65) degrees West five (5) chains to Station 5; thence North eighty-two and one-half (82½) degrees West seventy-three and one-half (73½) links more or less to a point bearing South

(Testimony of Mr. William E. Ware.)

twenty-one and three-fourths (21¾) degrees East one and fifty-four hundredths (1.54) chains from the point of beginning; thence North twenty-one and three-fourths (21¾) degrees West one and fifty-four (1.54) chains to place of beginning.

Excepting therefrom that portion thereof included in the one hundred (100) foot strip of land conveyed to the Los Angeles and Independence Railroad Company by deed recorded in Book 53, Page 553 of Deeds.

Also excepting that portion thereof described as follows:

Beginning at the intersection of the Northerly line of said one hundred (100) foot strip with the Westerly line of said Rancho; thence Easterly along said Northerly line two hundred ninety-eight (298) feet; thence at right angles Northerly eighty (80) feet; thence Westerly parallel with said Northerly line one hundred (100) feet; thence at right angles Southerly forty-four (44) feet; thence at right angles Westerly one hundred ninety-eight (198) feet; thence Southerly thirty-six (36) feet, more or less, to point of beginning.

Also excepting therefrom the Northerly two hundred feet thereof.

Parcel Two:

That parcel of land situate in the Rancho La Ballona, County of Los Angeles, State of California, described as follows:

Beginning at a point in the Southwest line of the County Road, said point being the most Northerly

(Testimony of Mr. William E. Ware.)

corner of the eighty-six and sixty-six hundredths (86.66) acre tract allotted to Andres Machado by final decree of partition in [86] case No. 2000 of the District Court of said County; thence along the Southwesterly line of said road, South thirty-nine (39) degrees East thirteen and twenty hundredths (13.20) chains to the point of intersection of a water ditch as it existed August 8th, 1887, with the aforesaid Southwest line of said road; thence Southeasterly along the line of said road one and seventy hundredths (1.70) chains; thence South thirty-seven and one-half (37½) degrees East sixty-seven (67) links to the line of a "wire and board fence" as recited in deed establishing the division line between the properties of C. B. Scott and Daniel M. McGarry recorded in Book 963, Page 257 of Deeds, Records of said County; thence following the line of said fence, South eighty-five (85) degrees thirty-eight (38) minutes West fifty-seven (57) links; thence South seventy-two (72) degrees four (4) minutes West two and sixty-three hundredths (2.63) chains; thence South sixty-three (63) degrees four (4) minutes West five and nine hundredths (5.09) chains; thence South thirteen (13) degrees twenty-six (26) minutes East seventy-four (74) links; thence South twenty-three (23) degrees nine (9) minutes West four and fourteen hundredths (4.14) chains; thence South sixteen (16) degrees fifty-four (54) minutes West four and nine hundredths (4.09) chains; thence South twenty-three (23) degrees

(Testimony of Mr. William E. Ware.)

thirty-eight (38) minutes West three and twelve hundredths (3.12) chains; thence South ten (10) degrees East seven and ninety-three hundredths (7.93) chains; thence South twenty-seven (27) degrees thirty-six (36) minutes West one and seventy hundredths (1.70) chains; thence South thirty-two (32) degrees fifty-nine (59) minutes West three and sixty-four hundredths (3.64) chains; thence South twenty-seven (27) degrees twenty-two (22) minutes West three and sixty-three hundredths (3.63) chains; thence South twenty-two (22) degrees forty-five (45) minutes West ninety-five (95) links, more or less, to a point which is South sixty-six (66) degrees thirty-five (35) minutes East one and twenty-hundredths (1.20) chains; from center line of Ballona Creek; thence North sixty-six (66) degrees thirty-five (35) minutes West one and twenty hundredths (1.20) chains to the center line of said Ballona Creek at the most Northerly corner of the tract of land marked "Augustin Cota 15.205 acres" on map showing part of said Rancho La Ballona recorded in Book 17, Page 77, Miscellaneous Records of said County; thence along the center line of said creek North fifteen (15) degrees East one (1) chain, more or less, to the Northeast corner of the thirty-four and ninety-hundredths (34.90) acre tract described in deed from D. M. McGarry and wife to Louis Salzeber, recorded August 1st, 1899, in Book 1301, Page 261 of Deeds; thence North fifty-five (55) degrees fifty-five (55) minutes West sixteen

(Testimony of Mr. William E. Ware.)

and forty hundredths (16.40) chains, more or less, to the Northwesterly line of said eighty-six and sixty-six hundredths (86.66) acre tract; thence along said Northwesterly line on a course of about North thirty-one and one-half (31½) degrees East thirty-eight and twenty-seven hundredths (38.27) chains, more or less, to the point of beginning. [87] including all buildings and improvements thereon or that may be hereafter erected thereon; together with all and singular the tenements, hereditaments and appurtenances, water and water rights, pipes, flumes and ditches thereunto belonging or in anywise appertaining, the reversion, remainder and remainders, rents, issues and profits thereof, for the purpose of securing:

First. The performance of the promises and obligations of this mortgage and the payment of the indebtedness evidenced by a promissory note (and any renewal or renewals thereof) in words and figures as follows:

$175,000.00

Los Angeles, California, November 12, 1929

Five years after date, for value received Artesian Water Company, a California Corporation, promises to pay to The Pacific Mutual Life Insurance Company of California, or order, at its office in Los Angeles, the sum of one hundred seventy-five thousand Dollars, with interest from date until paid, at the rate of six (6) per cent. per annum, payable

(Testimony of Mr. William E. Ware.)

quarterly, should the interest not be so paid, it shall become a part of the principal and thereafter bear like interest as the principal. Should default be made in the payment of any installment of principal or interest when due, then the whole sum of principal and interest shall become immediately due and payable at the option of the holder of this note. Principal and interest payable in lawful money of the United States. This note is secured by a mortgage upon real property of even date herewith.

[Corporate Seal] ARTESIAN WATER COMPANY
By M. K. RINDGE
President
By A. S. COOPER
Secretary

Second: The payment of such additional sums, with interest, as may hereafter be loaned by said mortgagee to said mortgagor or assigns, whether evidenced by promissory note or otherwise.

Third. The payment of attorney's fees in a reasonable sum to be fixed by the Court in any action brought to foreclose this mortgage, or in any action, suit or proceeding affecting the rights of the mortgagee herein, whether brought by or against the owner of said real property, involving either the title thereto, the lien of this mortgage thereon, the validity or priority of such lien, or any right of the mortgagee hereunder, whether such action, suit or

(Testimony of Mr. William E. Ware.)

proceeding progress to judgment or not; also the payment of all costs and expenses of such suit and also such sums as said mortgagee may pay for obtaining a policy of title insurance and for searching the title to the mortgaged property subsequent to the date of the recording of this mortgage or for surveying said property; also, whenever it becomes necessary for said mortgagee, in its judgment, to make any appearance in court in connection with the property herein mortgaged the payment of all court costs, and such attorney's fees as shall be paid, or agreed to be paid, by said mortgagee; all of which said sums, including said attorney's fees, are hereby declared a lien upon said property and are secured hereby.

Fourth. The payment of all sums expended or advanced by the mortgagee for taxes, assessments, encumbrances, adverse claims, fire, cyclone or tornado insurance, inspection, repair, cultivation, irrigation, protection, fertilization, fumigation or any other expenditure in connection with the care, preservation or maintenance of said property, or for any other purpose provided for by the terms of this mortgage.

The mortgagor agrees with said mortgagee to pay, as soon as due, all taxes, assessments, liens and encumbrances, which may be, or appear to be, liens upon said property or any part thereof, while the indebtedness, or any part thereof hereby secured, remains unpaid, including taxes levied or assessed

(Testimony of Mr. William E. Ware.)

upon this mortgage or upon the debt secured hereby, and hereby waives all right to treat the payment of such taxes or assessment as a payment on the debt secured hereby or as being to any extent a discharge thereof. [88]

And the mortgagor agrees to keep the buildings now erected or which may hereafter be erected on said premises, insured against loss by fire in an amount equal to the principal sum of said promissory note (or less if satisfactory to the mortgagee) in such companies as may be satisfactory to the mortgagee, the policies for such insurance shall be made payable, in case of loss, to said mortgagee, and shall be delivered to and held by it as further security; and that in default thereof, said mortgagee may procure such insurance, not exceeding the amount aforesaid, to be effected either upon its interest as mortgagee or upon the interest of the owner of the mortgaged premises, and in its name, loss, if any, being made payable to the said mortgagee, and may pay and expend for premiums for such insurance such sums of money as it may deem to be necessary; and the mortgagor further agrees promptly to pay and settle, or cause to be removed by suit or otherwise, all adverse claims against said property.

In case said taxes, assessments or encumbrances so agreed to be paid by the mortgagor be not so paid, or said buildings so insured and said policies so made payable, in case of loss, to said mortgagee,

(Testimony of Mr. William E. Ware.)

or said adverse claim so paid, settled or removed, then the mortgagee, being hereby made the sole judge of the legality thereof, may, without notice to the mortgagor, pay such taxes, assessments or encumbrances, obtain such policies of insurance, not exceeding the amount aforesaid, to be effected either upon its interest as mortgagee or upon the interest of the owner of the mortgaged premises, and in its name, loss, if any, being made payable to the said mortgagee, and pay or settle any or all such adverse claims, or cause the same to be removed by suit or otherwise.

The mortgagor agrees to keep said property in good condition and repair and to permit no waste thereof, and should said property, or any part thereof, require any inspection, repair, cultivation, irrigation, fertilization, fumigation, or protection, other than that provided by the mortgagor, then the mortgagee, being hereby made the sole judge of the necessity therefor, and without notice to the mortgagor may enter, or cause entry to be made, upon said property, and inspect, repair, cultivate, irrigate, fertilize, fumigate, or protect said property as it may deem necessary. All sums expended by the mortgagee in doing any of the things above authorized are secured hereby and shall be paid to the mortgagee by the mortgagor in said gold coin, on demand, together with interest from the date of payment, at the same rate of interest and in the same manner as is provided to be paid in the note hereinbefore set out.

(Testimony of Mr. William E. Ware.)

In the event of a loss under said policies of fire insurance, the amount collected thereon shall be credited first to the interest due, if any, upon said indebtedness, and the remainder, if any, upon the principal sum; and interest shall thereupon cease on the amount so credited on said principal sum.

The mortgagor hereby agrees, during the life of this mortgage, that, if application be made to have the premises described herein registered under the "Land Title Law," effective December 19, 1914, or any amendment thereof, or any other law governing the registration of titles to land, the mortgagor will at once repay all costs, expenses and attorney's fees incurred and deemed by the mortgagee to be necessary for the protection of its interests in connection with such applications; and all moneys advanced by the mortgagee for any such purposes, with interest at same rate as provided in the note or notes secured hereby, are hereby declared a lien upon said property. and are secured hereby. The mortgagor further agrees that, in case of such registration, said mortgagor will cause a certified copy of the certificate so issued, by virtue of such proceedings, to be delivered to the mortgagee as soon as issued.

The mortgagor promises to pay said note according to the terms and conditions thereof; and in case of default in the payment of same, or of any installment of interest thereon when due, or if default be made in the payment of any other of the

(Testimony of Mr. William E. Ware.)

moneys herein agreed to be paid, or in the performance of any of the covenants or agreements herein contained on the part of the mortgagor, the whole sum of money then secured by this mortgage shall become immediately due and payable at the option of the holder of said note, and this mortgage may thereupon, or at any time during such default, be foreclosed, and the filing of the complaint in foreclosure shall be conclusive notice of the exercise of such option by the mortgagee.

The plaintiff in such suit of foreclosure shall be entitled, without notice, to the appointment of a receiver, to collect and receive the rents, issues and profits of the mortgaged premises, and to exercise such other powers as the Court shall confer.

It is also agreed that should this mortgage be foreclosed, then in the decree of foreclosure entered in such action, the property described therein may be ordered sold en masse—or as one lot or parcel, at the option of the mortgagee.

And also, that the mortgagee may at any time, without notice, release portions of said mortgaged premises from the lien of this mortgage, without affecting the personal liability of any person for the payment of the said indebtedness or the lien of this mortgage upon the remainder of the mortgaged premises for the full amount of said indebtedness then remaining unpaid.

The mortgagor hereby mortgages the property hereinbefore described, to secure the performance

(Testimony of Mr. William E. Ware.)

of every promise and agreement herein contained, direct or conditional, and to secure the repayment to the mortgagee of all sums paid, laid out or expended by the said mortgagee under the terms of this mortgage, and also to secure the attorney's fees and costs provided for by this mortgage in case of a foreclosure thereof.

Every covenant, stipulation and agreement herein contained shall bind and inure to the benefit of said parties, their successors, heirs, executors, administrators or assigns.

Witness the corporate name and seal of the Mortgagor the day and year first above written, by its President and Secretary thereunto authorized.

ARTESIAN WATER COMPANY [Seal]

By M. K. RINDGE [Seal]
President

By A. S. COOPER [Seal]
Secretary

Signed and Sealed in Presence of

.....

.....

[Cancelled 7-25-38 R.N.D.] [89]

ORDER NO. [illegible]

When recorded please mail to The Pacific Mutual Life Insurance Company of California, Los Angeles, Cal.

COMPARED
Read by
NELSON
Document
HURST

[illegible] TRUST CO.

NOV 25 1929 [illegible] M.
Book 2526 Page [illegible]
Official [illegible]
Recorder, Los Angeles County, Cal.
Deputy.

4100
36

No. 3509

Mortgage

TO

The Pacific Mutual Life Insurance Company of California

PACIFIC MUTUAL BUILDING
Los Angeles, California

STATE OF California
COUNTY OF Los Angeles } ss.

On this 22 day of November in the year of our Lord, one thousand nine hundred and Twenty-nine before me, Irma E. Konsiva, a Notary Public in and for said County of Los Angeles residing therein, duly commissioned and sworn, personally appeared M. K. Ridge, known to me to be the President, and A. M. Cooper known to me to be the Secretary of Artesian Water Company the corporation described in and that executed the within instrument, and known by me to be the persons who executed the within instrument on behalf of the corporation therein named, and acknowledged to me that such corporation executed the same.

IN WITNESS WHEREOF, I have hereunto set my hand and affixed my Official Seal, the day and year in this certificate first above written.

Irma E. Konsiva
Notary Public in and for the County of Los Angeles State of California
[CORPORATION] My commission will expire Nov 7, 1931

STATE OF
COUNTY OF } ss.

On this day of in the year of our Lord, one thousand nine hundred and before me, , a Notary Public in and for said County of residing therein, duly commissioned and sworn, personally appeared

known to me to be the person whose name subscribed to the within instrument, and acknowledge to me that he executed the same.

IN WITNESS WHEREOF, I have hereunto set my hand and affixed my Official Seal, the day and year in this certificate first above written.

Notary Public in and for the County of State of
[GENERAL] My commission will expire

U. S. BOARD OF TAX APPEALS
DIV. 15 DOCKET 100824
ADMITTED IN EVIDENCE
JUN 11 1940
PETITIONER'S EXHIBIT 4
RESPONDENT'S

(Testimony of Mr. William E. Ware.)

By Mr. Witter:

Q. Now, did the mortgage that was given to secure these notes comprise substantially all of the properties of value of the Artesian Water Company, or otherwise?

A. I believe the property known as the Home Villa property was not included, which is a subdivision property. But it represents substantially the major portion of the assets of the company, yes.

Q. Does the mortgage include all of the income-producing properties of the company with respect to the year 1937, the taxable year? A. Yes.

[47]

Q. Now, these notes matured on November 12, 1934. Were they paid on that date, Mr. Ware?

A. They were not.

Q. And on what date were you appointed receiver? A. July 16, 1935.

Q. Had any payment been made upon these notes at the time you were appointed receiver?

A. No.

Q. What steps did you take, if any, to effect any payment upon these notes as receiver?

A. During the year 1936 I attempted to secure an extension of time on these notes and submitted a proposal to Mr. Green, who was then the head of the Mortgage Loan Department of the Pacific Mutual, proposing the payment of I believe it was $20,000 on the then indebtedness, and amortize it at the rate of $2750 a month, plus interest.

(Testimony of Mr. William E. Ware.)

Negotiations continued for some little time to take the matter up with the Board, but in the interim, while these negotiations were going on the conservator was appointed for the Pacific Mutual Life Insurance Company. This loan was severely criticised by the conservator because of certain interlocking interests. Mr. George Cochran, who was then the president of the Pacific Mutual Life Insurance Company and Mr. Samuel Ringe, who was a member of the Board of Directors of the Pacific Mutual [48] Life Insurance Company, Mr. Lee Phillips, and Mr. Stanley McLung were all interested in the Artesian Water Company as stockholders. The conservator felt that inasmuch as there was this interlocking interest that the loan should be paid immediately, and so called the loan.

I then tried to secure a further extension of time in order to attempt to refinance, if possible. The results of these discussions were that the Pacific Mutual, the conservator for the Pacific Mutual Life Insurance Company, stated that they would give me until March of 1937 to refinance the loan, at which time if I was unsuccessful they would expect full payment.

I attempted to approach various brokers and banks for a refinancing but was met with the objection that the company being in receivership they were afraid that proper title could not be passed and that who would be available to sign the mortgage loan or create the indebtedness.

(Testimony of Mr. William E. Ware.)

In the meantime, I had been negotiating with the Shell Oil Company, who were the owners of the lease, in an effort to get them to further exploit the——

Q. Pardon me. I will introduce the correspondence you had with respect to extending the time for payment.

The Clerk: This document will be marked for identification Petitioner's Exhibit No. 5. And this will be marked Petitioner's Exhibit No. 6. [49]

(The said documents so offered were marked Petitioner's Exhibits 5 and 6 for identification.)

By Mr. Witter:

Q. Mr. Ware, I show you what has been marked for identification Petitioner's Exhibit No. 5, and I will ask you to state what it is.

A. This represents a copy of a letter written by myself as receiver to the Pacific Mutual Life Insurance Company under date of July 17, 1936 in which the matter of the unpaid principal balance of $175,000 and $35,000 respectively were discussed.

Mr. Witter: Your Honor doesn't care to have these letters read?

The Member: If they are introduced as exhibits it won't be necessary.

Mr. Witter: I will offer in evidence then Petitioner's Exhibit No. 5.

Mr. Tonjes: No objection.

(Testimony of Mr. William E. Ware.)

The Member: It will be received as Petitioner's Exhibit No. 5.

(The document so offered and received in evidence, was marked Petitioner's Exhibit 5, and made a part of this record.) [50]

PETITIONER'S EXHIBIT No. 5

650 South Grand Avenue

July 17, 1936

Pacific Mutual Life Insurance Company
523 West Sixth Street
Los Angeles, California
Attention—Mr. Green:

In re: Artesian Water Company

Gentlemen:

You will recall that a short time ago you requested that I discuss with you the matter of the loans heretofore made by you to the Artesian Water Company, upon which there remain unpaid principal balances of $175,000 and $35,000 respectively. Such loans are now in default as to principal and you have suggested that some arrangement be made to correct such defaults.

I have considered the matter in detail with a view to ascertaining what course the company can adopt to satisfy your requirements. You understand, of course, that as receiver for the company I have no power to make any commitments on its behalf, but must submit any tentative arrangements which we may make to the superior court, and that

(Testimony of Mr. William E. Ware.)

I desire to secure the consent of the board of directors of the company to any proposed settlement. I am inclined to believe, however, that I might be able to obtain the approval of the board of directors and the court of the payment of $10,000 for application upon the principal of one or the other obligation and a new plan contemplating the payment of the balance of $200,000 in five years with interest at the rate of five per cent per annum, payable quarterly. Since the company desires to liquidate its indebtedness at the earliest possible moment, such plan should make provision for the payment of any multiple of $1,000 upon any quarterly interest date without penalty.

I further believe that, under present conditions, the company could pay about $6,000 quarterly on account of principal and in the absence of unforseen events should continue so to do.

In the event the above suggestions are not satisfactory to you, I would be happy to have the benefit of your ideas in the matter. Will you kindly communicate with me at your convenience.

Very truly yours,

WILLIAM E. WARE

Receiver—Artesian Water Company

WEW:M

C.C. to—

Mr. Marvin Osburn

Mr. Sam Rindge

Mr. William Larrabee

[Endorsed]: Petitioner's Exhibit No. 5. Admitted in evidence June 11, 1940. [91]

(Testimony of Mr. William E. Ware.)

By Mr. Witter:

Q. I show you what has been marked for identification Petitioner's Exhibit No. 6 and ask you if that is the reply of the Pacific Mutual Company to the letter marked Petitioner's Exhibit No. 5 which you yourself wrote.

A. This is a reply to my letter. But there were some discussions in the interim between the dates of this letter and this letter, which were more or less informal discussions with the Pacific Mutual Life Insurance Company.

Mr. Witter: I offer in evidence Petitioner's Exhibit No. 6.

Mr. Tonjes: No objection.

The Member: It will be received as Petitioner's Exhibit No. 6.

(The said document so offered and received in evidence, was marked Petitioner's Exhibit 6, and made a part of this record.)

(Testimony of Mr. William E. Ware.)

PETITIONER'S EXHIBIT No. 6

Pacific Mutual Life Insurance Company

Los Angeles, California
September 14, 1936

6509—Artesian Water Company

Artesian Water Company
650 South Grand Avenue
Los Angeles, California

Attention: William E. Ware, Receiver

Gentlemen:

Please be referred to the above numbered loan standing at an unpaid principal balance of $210,000, which has been running past due since November 12, 1934, and which is secured by mortgage recorded in Book 9596, page 14, of Official Records, Los Angeles County, California.

Subject to our being able to obtain court authority to so do, we shall extend informally the time for payment of this obligation until March 2, 1937, provided—

(1) That you pay us within fifteen days from this date the sum of $18,500 in cash, and $3,500 on the first day of each month during said extension period commencing October 1st next, said sums as received to be applied toward liquidation of the principal of this obligation; and

(2) That interest is to be at the rate of six (6) per cent. per annum from August 12, 1936,

(Testimony of Mr. William E. Ware.)

payable quarterly, and the extension is to be subject otherwise to compliance with all terms of the original note and mortgage.

We are instructed to inform you that no further extensions of time for payment of this loan will be granted after March 2, 1937, and you will kindly make arrangements to retire this obligation not later than said date.

Very truly yours,

PACIFIC MUTUAL LIFE INSURANCE COMPANY

By JOHN B. COOLEY,

Manager Mortgage Loan Department.

JBC/D

[Endorsed]: Petitioner's Exhibit No. 6. Admitted in evidence June 11, 1940. [92]

By Mr. Witter:

Q. Going back just a moment.

When these notes matured in 1934, Mr. Ware, if you know, was there a request for an extension of time made upon Pacific Mutual Company, and was that request refused?

A. I was not present. I don't know of my own knowledge that that was done except from subsequent correspondence and reference to notations I found in the file, [51] that was the case.

Q. In Petitioner's Exhibit 6, which is the response to your letter to the Pacific Mutual Company

(Testimony of Mr. William E. Ware.)

requesting extension of time, they give you until March 3, 1937 to make payment in full. Were you able to make payment in full on that date?

A. I was not.

Q. Did you make strenuous efforts to meet their terms laid down in that letter? A. I did.

Q. And were you wholly unable to meet the terms that they laid down in that letter?

A. I was.

Q. Now, the total indebtedness of these notes in principal amount at the time you became receiver was $210,000, is that correct?

A. That is correct.

Q. In the year 1936, how much were you able to pay off on that principal?

A. Approximately $25,000.

Q. So that on January 1, 1937 there was approximately $185,000 still due on the principal indebtedness? A. That is correct.

Q. And during the year 1937 how much were you able to reduce this $185,000 still owing? [52]

A. May I see the company's tax returns?

(The document referred to was passed to the witness.)

The Witness: It was reduced to a balance of $100,250.

By Mr. Witter:

Q. What did the income of the company consist of?

(Testimony of Mr. William E. Ware.)

A. Approximately ninety per cent of it was from the royalties of the oil lease.

Q. Did at least ninety-seven per cent consist of oil royalties?

A. I didn't figure the percentage, but it could be.

Q. Is it true that substantially all of the income consisted of oil royalties? A. That is true.

Q. I will ask you whether or not the total oil royalties from any oil leases that the company had had been assigned to the Pacific Mutual Company?

A. They had.

Q. And had the Pacific Mutual Company merely permitted the Artesian Water Company to collect the royalties during such time as it saw fit to do so under that assignment?

A. That is correct.

Q. Mr. Ware, what was the condition of the Artesian Water Company at the beginning of the taxable year so far as [53] undivided profits or an operating deficit were concerned?

Mr. Tonjes: That is objected to, Your Honor, as calling for a conclusion and not the best evidence.

The Member: Well, I would think of course that the best evidence would be the books of the corporation. Did they have a balance sheet at that time?

Mr. Witter: Well, if Your Honor please, he was in the position of a taxpayer himself. He is an auditor. Could not he know of his own knowledge that a deficit or an undivided surplus existed on that date?

(Testimony of Mr. William E. Ware.)

The Member: Well, that is probably true, yet I should think that it would be a little risky to have a witness testify from memory as to just what that is. It seems to me that the best evidence would be the balance sheet of the company. Isn't that available?

Mr. Witter: It is on the income tax return. He possibly has it among his papers.

Do you have it, Mr. Ware?

The Witness: I don't have it in 1936. It is on the tax return.

The Member: If it is on the tax return he can read it as shown by the tax return.

By Mr. Witter:

Q. To refresh your recollection then, I will show you the balance sheet that accompanied the 1937 return filed by [54] the company and ask you whether or not there was a deficit at the beginning of the taxable year 1937, and if so how much?

A. There was a deficit of $50,571.90.

The Member: That is as shown by the balance sheet attached to the 1937 income tax return as filed and examined by the department.

By Mr. Witter:

Q. And at the end of the taxable year that deficit had been reduced? A. It had.

Q. And what was the condition?

A. There was an undistributed profit of $34,442.50.

The Member: Instead of a deficit?

(Testimony of Mr. William E. Ware.)

The Witness: Instead of a deficit. At the close of the year.

By Mr. Witter:

Q. While you were receiver for the company, did you have to obtain an order of the Court for any transaction of any consequence that took place?

A. Yes.

Q. Whenever you made a payment upon one of these notes, for instance, did you have to obtain an order of the Court? A. I did. [55]

Q. Were you wholly under the supervision of the Court in everything that you did?

A. I was.

Q. Did you take any action that wasn't supported either specifically or generally by an order of the Court? A. I did not.

Mr. Witter: I will ask that this be marked for identification, Mr. Clerk.

The Clerk: It will be marked Petitioner's Exhibit 7 for identification.

(The said document so offered, was marked Petitioner's Exhibit 7, for identification.)

By Mr. Witter:

Q. I hand you what has been marked for identification Petitioner's Exhibit 7 and ask you if that is a copy of an order that you obtained from the Court for making a payment upon the notes owned by the Pacific Mutual Company. A. It is.

Q. And is that a representative order such as

(Testimony of Mr. William E. Ware.)

you obtained each time you made any payment upon these notes? A. It is.

Mr. Witter: I offer in evidence Petitioner's Exhibit No. 7.

Mr. Tonjes: No objection. [56]

The Member: It will be received in evidence as Petitioner's Exhibit No. 7.

(The said document so offered and received in evidence, was marked Petitioner's Exhibit 7, and made a part of this record.)

PETITIONER'S EXHIBIT NO. 7

In the Superior Court of the State of California in and for the County of Los Angeles

No. 390338

J. C. BALDWIN,

Plaintiff,

vs.

FREDERICK H. RINDGE, et al.,

Defendants.

ORDER AUTHORIZING RECEIVER TO MAKE PAYMENT ON PRINCIPAL OF NOTE SECURED BY MORTGAGE AND ASSIGNMENT OF LEASES.

The Petition of Receiver for Instructions and Authority to Make Payment on Principal of Note Secured by Mortgage and Assignment of Leases, dated February 18, 1938, filed by the receiver here-

(Testimony of Mr. William E. Ware.)

in, coming on regularly for hearing on February 23, 1938, in Department 34 of the above entitled court, and it appearing that due and legal notice of the time and place of the hearing of said petition has been given to all the parties interested herein, and no person appearing to oppose the same, and evidence having been introduced in support of said petition,

It Is Hereby Ordered that said petition be granted, and that William E. Ware, as receiver for the Artesian Water Company, a corporation, is instructed and authorized to make payment, at this time, of Thirty Thousand Dollars ($30,000.00), on account of the principal of the indebtedness described in his petition, to Pacific Mutual Life Insurance Company, a corporation; said payment to be in excess of the monthly payments of Twenty-seven Hundred Fifty Dollars ($2,750.00) being made by him, as described in said petition.

Dated: February 23, 1938.

WILSON

Judge

[Endorsed]: Petitioner's Exhibit No. 7. Admitted in evidence June 11, 1940. [93]

Mr. Witter: Mr. Clerk, will you mark this document for identification?

The Clerk: It will be marked for identification as Petitioner's Exhibit No. 8.

(Testimony of Mr. William E. Ware.)

(The said document so offered was marked Petitioner's Exhibit 8, for identification.)

By Mr. Witter:

Q. I hand you what is marked for identification Petitioner's Exhibit No. 8 and ask you if that is a true copy of the by-laws of the Artesian Water Company.

A. It appears to be the copy of the by-laws as I saw them.

Mr. Tonjes: Do you know, Mr. Ware?

The Witness: I haven't compared it.

Mr. Witter: I didn't compare it with the original. It was given to me by the taxpayer company as a true copy of the by-laws of the corporation. I don't desire to introduce it in evidence. I merely desire to read into the record one provision which states the powers of a director [57] so far as declaring dividends is concerned.

Mr. Tonjes: I don't like to object to the competency of the document, Your Honor, but I will object to the offer.

The Member: Go ahead and make your offer.

By Mr. Witter:

Q. Mr. Ware, you have seen the original by-laws of the company? A. I have.

Q. And you are familiar with them and their contents? A. I have read them, yes.

Q. Well, I will ask you to read Petitioner's Exhibit 8 and state whether or not that is a true copy.

A. This appears to be a copy of the by-laws.

(Testimony of Mr. William E. Ware.)

Q. Mr. Ware, calling your particular attention to the second paragraph in Article 5 of the by-laws, I will ask you if you recall that that is a true copy of the provision.

A. I would say it was, yes, because I have read that several times in connection with this matter.

Q. That purports to state the powers of the directors so far as declaring dividends is concerned? A. Yes.

Q. And this is a correct copy of what appears in the original so far as that power is concerned?

A. Yes. [58]

Mr. Witter: If Your Honor please, I do not desire to introduce this entire document because there is only one sentence here that has any bearing on the case.

I would like to read that into the record.

Mr. Tonjes: That is objected to, Your Honor, on the ground that it is incompetent. I will waive the objection with respect to competency. It is immaterial. That the by-laws of a corporation have never been held to be a contract which would either restrict or not restrict the payment of dividends by a corporation in so far as it applies to a contract under the provisions of the Revenue Act.

The Member: I will overrule the objection.

Mr. Witter: Article 5 of Petitioner's Exhibit 8, which purports to be a true copy of the by-laws of the Artesian Water Company, reads as follows: "Duties of Directors. It shall be the duty of di-

(Testimony of Mr. William E. Ware.)

rectors (second) to declare dividends out of the surplus profits when such profits shall in the opinion of the directors warrant the same."

If Your Honor please, from a recent case it appeared that the Board of Tax Appeals did not take judicial notice of the code provisions of a state.

The Member: That is news to me.

Mr. Witter: It was news to me. [59]

Because of what I inferred from that recent decision, I came prepared to prove the laws of this state with respect to certain matters in this case. But if the Board takes judicial notice of those statutes then that proof isn't necessary.

The Member: We always have.

I am not aware of any decision of the Board that holds it is necessary to introduce into evidence the statute of the state or of the United States. Of course when it comes to a foreign law that has to be proved. But I think you surely must be mistaken as to any Board case.

Mr. Witter: It wasn't a Board decision, Your Honor. I am sorry I don't recall exactly which one it was. But it was on appeal.

The Member: I certainly have always taken judicial notice of the code of the state.

Mr. Tonjes: If Your Honor please, to clarify things, I will be willing to stipulate the Board might take judicial notice of all of the states' statutes.

(Testimony of Mr. William E. Ware.)

The Member: Yes.

That will be stipulated although I think it is unnecessary. However, you may note it in the record.

Mr. Witter: If Your Honor will bear with me for just a moment, I think I will be through. [60]

By Mr. Witter:

Q. Mr. Ware, you have stated the operating deficit that existed at the beginning of the year and the amount of undivided profits at the end of the year. I will ask you whether or not in arriving at those amounts that you have stated any deduction was taken for depletion.

Mr. Tonjes: That is objected to as being immaterial, Your Honor.

The Member: Well, I will overrule the objection. I am not prepared to say it would be immaterial at this time.

The Witness: There was not.

By Mr. Witter:

Q. Virtually all of the income that reduced the deficit was income derived from oil royalties?

A. Yes.

Q. And yet no depletion deduction was taken?

A. In the surplus account.

Q. I will ask you if you are able to say, in your opinion, as an auditor and as a receiver for the company in the taxable year, if the proper deduction had been taken for depreciation would

(Testimony of Mr. William E. Ware.)

there have been any undivided profits balance at the end of the taxable year?

A. May I see the return?

(The document referred to was passed to the witness.) [61]

The Witness: There would have been no surplus without depletion. I say there would have been no depletion surplus if depletion had not been credited back to surplus.

Mr. Tonjes: I ask that the answer be stricken and the witness re-answer the question.

The Member: If he can give the gross income from oil royalties, why then it would be a mathematical calculation I suppose to figure what the depletion would be, the percentage depletion was.

The Witness: In order to answer that question, the tax return for the year shows an undivided profit at the end of the year of $34,442.50. If that was reduced by the depletion of $44,863.38 there would be a deficit of approximately $10,400.

The Member: That is a better way to state it. That gives the figures.

By Mr. Witter:

Q. Suppose the depletion had been figured on a cost-depletion basis, are you able to state whether there would have been undivided profits at the end of the year? A. I wouldn't.

Q. Would the undivided profits at the end of the year then have been materially reduced?

(Testimony of Mr. William E. Ware.)

A. They would. [62]

Q. They would if depletion had been taken on a cost basis? A. That is right.

Q. Now, during the year 1937, when you were receiver for this company, I ask you, Mr. Ware, if you were able to make adequate provisions for meeting the debts and liabilities of the Artesian Water Company?

Mr. Tonjes: That is objected to, Your Honor, as calling for a conclusion.

The Member: I will overrule the objection.

The Witness: May I have the question?

(Whereupon, the reporter read the question as recorded.)

By Mr. Witter:

Q. As they matured? A. I was not.

Mr. Witter: That is all.

Cross Examination

By Mr. Tonjes:

Q. Mr. Ware, you stated that you were unable to meet or make arrangements for payment of debts as they matured. Which debts matured which could not be met?

A. The Pacific Mutual debts.

Q. Did you make arrangements with them to extend the time?

A. There was no definite arrangement as to extension. [63]

(Testimony of Mr. William E. Ware.)

Q. Did they take any legal proceedings against the corporation?

A. They started to take legal proceedings and then due to their own difficulties on some of their own matters they deferred the action with a more or less of a reservation that practically all of the income of this company would be diverted to them.

Q. Did the company become involved in any legal proceedings on account of its inability to pay its bills? A. No.

Q. And to the best of your knowledge all of its bills were paid?

A. Except this one obligation that was past due.

Q. That obligation was somewhat past due?

A. Yes. This obligation was past due since 1934.

Q. Now, what efforts did you make to obtain funds to refinance the loan to the Pacific Mutual Company?

A. I approached the loaning officers of the California Bank, the Security First National Bank, and two or three other bankers in town with the idea of attempting to put a new loan on to take the Pacific Mutual out.

Q. And what was the outcome of those negotiations?

A. They all fell through due to the fact that none of the loaning officers felt that they could make a new loan signed by the receiver. The title companies, in [64] other words, would not issue title satisfactory to the loaning agency.

(Testimony of Mr. William E. Ware.)

Q. It was more on account of a lack of ability to give good collateral in that they couldn't pass good title rather than the value of the collateral, is that correct?

A. No, I wouldn't say that because the value was more or less unknown. I recall that in the negotiations with the Security Bank they spent considerable time in the appraising. They had some idea of the values of these properties. They felt that because of the fact the title company couldn't be brought down that they wouldn't go any further with it. But I don't know the exact figures that they used in connection with their investigation.

Q. But the company did produce sufficient oil to have paid to them in the year 1937 royalties in the amount of $175,000, is that correct?

A. Whatever the tax return shows. I don't have the information in front of me.

Mr. Witter: Do you mean gross royalties received, Mr. Tonjes?

Mr. Tonjes: Yes.

Q. I will amend my statement. I will change that figure to royalties in the amount of $163,139.56. Would you say that that is correct? A. Yes.

[65]

Q. And the company also had some other items which produced income, did it not? A. It did.

Q. And that was in the form of rents?

A. Some rents, some interest.

(Testimony of Mr. William E. Ware.)

Q. And what was the nature of the property which produced the rents?

A. Some houses on Home Villa tract principally, and there were also some rentals from farming leases on the vacant acreage, and some rental from the Asphalt Paving Company which had a portion of the property on the Sentous property.

Q. Did the income from such properties during 1937 amount to $8,353.86?

Mr. Witter: Is that gross income, Mr. Tonjes?

The Witness: Yes. That is the gross income from rentals.

By Mr. Tonjes:

Q. Do you know whether or not the property producing these rentals was incumbent?

A. Some of it was and some of it was not. The portion that produced the major portion of that revenue was incumbent.

Q. Can you show me on the balance sheet of the corporation wherein the incumbrances against such properties [66] are recorded?

A. They are under the item of Bonds, Notes, Mortgages Payable, Item 12 on the balance sheet.

Q. Does that include the indebtedness to the Pacific Mutual Company? A. It does.

Q. How much of it relates to the Pacific Mutual Company's indebtedness and how much to others, if you know?

A. At the end of 1937 the only indebtedness was due to the Pacific Mutual Life Insurance Com-

(Testimony of Mr. William E. Ware.)

pany. There was no other indebtedness on mortgage loans.

Q. Then the Pacific Mutual Company was a creditor and held license on both the oil property and the other properties of the Artesian Water Company, is that correct? A. That is correct.

Q. The corporation carries on its balance sheet an item Land and Buildings carried at a figure of somewhat in excess of one million dollars at the beginning of the taxable year, and $999,000 at the close of the taxable year. Did you know the circumstances under which the properties in question were valued?

A. Yes. Most of the values appearing on the books are based upon the March 1, 1913 values of the properties of the company.

Q. Would you say that that March 1, 1913 value and [67] the value in 1937 were substantially different?

A. Well, I am not a real estate man and I cannot appraise values. I wouldn't know. I would say there would be a substantial difference based upon sales that were actually made.

Q. Would you say the value was greater in 1937 than in 1913, or less?

A. The value in 1937 would be less than in 1913.

Q. Would be less? A. Yes.

Q. And on what do you base such an opinion?

A. Largely upon the sales of property that were

(Testimony of Mr. William E. Ware.)

made in the subsequent years showing losses over the values of 1913.

Q. Now, when the Pacific Mutual Company advanced money to the Artesian Water Company did the Artesian Water Company assign to the Pacific Mutual Company the Shell Oil lease?

A. It did.

Q. And under the terms of that lease, or under the terms of that loan rather, did the Shell Oil Company continue to pay all of the royalties to the Artesian Water Company? A. It did.

Q. And that was true during the entire year 1937? [68] A. That is right.

Q. Now the Artesian Water Company you say became involved in a receivership proceeding. Was that in the year 1934? A. 1935.

Q. Will you explain to the Board the circumstances of that receivership proceeding?

A. That receivership arose out of an action by one J. Baldwin against Frederick Ringe who was a stockholder of the Artesian Water Company. It appeared that Baldwin had a judgment of some $200,000 against Frederick Ringe. After considerable investigation they located a safe deposit box in Stockton, California, and in this box there were some stock of the Artesian Water Company, some of the Marblehead Land Company, and some of the Ringe Company. The stock was acquired by Baldwin under sheriff's sale and application was made to these corporations to have the stock trans-

(Testimony of Mr. William E. Ware.)

ferred to Baldwin. The corporate officers refused to transfer the certificates and counsel for Baldwin petitioned the Superior Court of this county for the appointment of a receiver ex parte, on the grounds that the corporate officers were not functioning under the code.

Under that action the Court appointed me as receiver.

Q. And in that connection was the question of in- [69] solvency or was the insolvency of the Artesian Water Company in any way involved?

A. I believe one of the grounds in the application for the receiver alleged fraud and conspiracy and mismanagement on the part of the corporation.

Q. This was not an action brought by a creditor against the corporation?

A. No, it was not. It was a stockholder presumably.

Q. When were you appointed receiver?

A. July 16, 1935.

Q. And when did you terminate your receivership? A. February 8, 1939.

Q. Now, what efforts were made in the meantime to have the receivership terminated by the stockholders?

A. At the original appointment an appeal was filed on the appointment of the receiver. An amended complaint was filed I believe in October of 1936, if my memory serves me. And in the amended complaint an allegation was set up I believe. There was

(Testimony of Mr. William E. Ware.)

a deadlock on the board. I was discharged under the original appointment and reappointed under the amended complaint.

Q. Then as I get it, neither the appointment of the receiver nor the continuation of the receivership was brought about by reason of the inability of the company to pay its bills, is that correct? [70]

A. Not brought about by that, no. But because of the negotiations that were going on with the Pacific Mutual Life Insurance Company for the extension of this loan, there was a more or less of a desire on the part of the corporation itself to permit the receiver to continue because they themselves in taking part would have been faced with the immediate calling of that loan and the assignment of all the income; while as long as the receiver was in and in control of the property the Pacific Mutual Life Insurance Company felt that whatever funds were coming to the company would be paid to them on their loan; and they virtually made the statement to one of the directors at one time that if the receivership were discontinued they would expect to immediately start action.

Mr. Tonjes: I think that is all.

Redirect Examination

By Mr. Witter:

Q. Mr. Tonjes has called to your attention certain rental income received by the company. I ask you to look at a copy of the income tax return and

(Testimony of Mr. William E. Ware.)

state any deductions that are taken on that return that would apply against that rental gross income.

A. Well, there is $4518.05 for the repairs and some depreciation.

Q. How much depreciation? [71]

A. $3352.92 out of $3425.92.

Q. And is there a tax deduction for taxes, State and County taxes? A. There is.

Q. How much is that?

A. Well, the total tax deduction is $26,533.70.

Q. Would a portion of that apply to the rental properties? A. It would.

Q. Mr. Ware, you testified about your efforts to get finances with which to meet the demands of the Pacific Mutual Company. Were your efforts hampered and embarrassed by the fact that the notes were already over two years in default?

A. Oh, yes, that objection was brought up continually.

Q. Were they hampered also by the fact that the company was in receivership? A. Yes.

Q. What steps, if any, did you take—I will withdraw that question.

As an auditor, are you quite familiar with tax procedure? A. Fairly so.

Q. Income tax procedure, Mr. Ware?

A. Yes. [72]

Q. As a receiver of this company, and in view of your familiarity and experience with income tax matters, what steps or precautions did you take,

(Testimony of Mr. William E. Ware.)

if any, to ascertain whether or not there would be any imposition of an undistributed profits tax in this case.

Mr. Tonjes: That is immaterial, Your Honor. I object to it.

The Member: What do you expect to show, Mr. Witter?

Mr. Witter: I really think it is immaterial, if Your Honor please.

The Member: I will sustain the objection.

Mr. Witter: That is all for the petitioner.

Mr. Tonjes: That is all, Mr. Ware.

The Member: Very well, you are excused.

Witness excused.

The Member: Do you gentlemen wish to submit this case on brief?

Mr. Witter: I would prefer to, Your Honor, I would like to submit a short brief.

The Member: Is that all of your evidence?

Mr. Witter: I think it might be helpful to introduce the return for the year 1937.

Mr. Tonjes: I think it might be, Your Honor.

Mr. Witter: There are some details shown in the [73] return that aren't reflected in that data.

The Member: It will be received as Petitioner's Exhibit No. 9.

(The said document so offered and received in evidence, was marked Petitioner's Exhibit 9, and made a part of this record.)

UNITED STATES

1937 CORPORATION INCOME AND EXCESS-PROFITS TAX RETURN 1937

Treasury Department (FORM 1120) Internal Revenue Service

For Calendar Year 1937 or Fiscal Year

beginning ....., 1937, and ended ....., 1938

File Code 5 1

Serial No. 402482

District .....

(Collector's Stamp)

RECEIVED WITH REMITTANCE

Cash Check M. O.

First Payment $ .....

PRINT PLAINLY CORPORATION'S NAME AND ADDRESS

William E. Ware, Receiver for Artesian Water Co.
(Name)

727 West Seventh Street - Room 544
(Street and number)

Los Angeles (Post office) Los Angeles (County) California (State)

Kind of business: Land Owners

EXCESS-PROFITS TAX COMPUTATION

Item No.			Rate	Amount of Tax
1.	Net income for excess-profits computation (item 28, Schedule A)	$ Exempt (See Treasury Dept letter of 1-20-38 Re:-MT:CST:JMB - 351831 - Signed by D. S. Bliss, Deputy Comm'r.)		
2.	State value of capital stock as declared in your capital stock tax return for the year ended June 30, 1937 (or in your capital stock tax return for the year ended June 30, 1938, if your income tax fiscal year began in 1937 and ended on or after July 31, 1938) $			
3.	Enter here 10 percent of item 2 $			
4.	Dividends received credit (85 percent of Schedule F, column 2)			
5.	Balance subject to excess-profits tax (item 1 minus items 3 and 4)	$		
6.	Amount taxable at 6 percent (5 percent of item 2, but not more than item 5)		6%	$
7.	Balance taxable at 12 percent (item 5 minus item 6)	$	12%	
8.	Total excess-profits tax			None

NORMAL TAX COMPUTATION

9.	Net income for income tax computation (item 31, Schedule A)	$ 54,101 14		
10.	Dividends received credit (85 percent of Schedule F, column 2) $			
11.	Dividends paid credit (for mutual investment companies)			
12.	Balance subject to normal tax (item 9 minus item 10 or 11)	$ 54,101 14		
13.	Tax on portion of item 12 not in excess of $2,000	$ 2,000 00	8%	$ 160 00
14	Tax on portion of item 12 in excess of $2,000 and not in excess of $15,000	13,000 00	11%	1,430 00
15.	Tax on portion of item 12 in excess of $15,000 and not in excess of $40,000	25,000 00	13%	3,250 00
16.	Tax on portion of item 12 in excess of $40,000	14,101 14	15%	2,115 17
17.	Total normal tax in items 13 to 16			$ 6,955 17
	NORMAL TAX ON CORPORATIONS NOT SUBJECT TO GRADUATED RATES (to be used in lieu of the normal tax rates above)	Item 12 above		
18.	Banks and trust companies (see Instruction II)	$	15%	$
19	Insurance companies		15%	
20	Corporations entitled to the benefits of section 251 of the Revenue Act of 1936		15%	
21	Corporations organized under the China Trade Act, 1922		15%	
22.	Foreign corporations engaged in trade or business within the United States not having office or place of business therein		22%	

UNDISTRIBUTED PROFITS TAX COMPUTATION

(See Instruction III regarding corporations exempt from surtax)

23	Net income for income tax computation (item 31, Schedule A)	$ 54,101 14		
24.	Normal tax (item 17 above)	$ 6,955 17		
25.	Credit for holding company affiliate or national mortgage association (see Instruction III (b) and (c))	6,955 17		
26.	Adjusted net income (item 23 minus items 24 and 25)	47,145 97		
27	Dividends paid credit (line 13, Schedule M) $			
28.	Credit for contracts restricting dividend payments (see Instr. III)	8,250 00		
29	Undistributed net income (item 26 minus items 27 and 28)	$ 38,895 97		
30.	Portion of item 29 taxable at 7½: $5,000 or 10% of item 26, whichever is greater (but not more than item 29)	$ Exempt - See attached statement		
31.	Portion of item 29 taxable at 12½: 10% of item 26 (but not more than item 29 minus Item 30)		12½	
32	Portion of item 29 taxable at 17½: 20% of item 26 (but not more than item 29 minus items 30 and 31)		17½	
33.	Portion of item 29 taxable at 22½: 20% of item 26 (but not more than item 29 minus items 30 to 32)		22½	
34.	Portion of item 29 taxable at 27½: (item 29 minus items 30 to 33)		27½	
35.	Total surtax in items 30 to 34			$ None
36.	Total normal tax and surtax (item 17 plus item 35, or item 18, 19, 20, 21, or 22)			$ 6,955 17
37.	Less: Credit for income tax of a foreign country or U. S. possession allowed a domestic corporation (see Instruction IV)			
38.	Balance of tax (item 36 minus item 37)			$ 6,955 17
39.	Excess-profits tax (item 8 above)			None
40	Total tax due (item 38 plus item 39)			$ 6,955 17

NOTE.—One form marked "DUPLICATE COPY" must be filed with this original return ($10 will be assessed if duplicate copy is not filed).

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Item and Instruction No.				
1. Gross sales (where inventories are as income-determining factor)	Less returns and allowances $	$		
2. Less cost of goods sold (Schedule D-1)				
3. Gross profit from sales (Item 1 minus Item 2)		$		
4. Gross receipts (where inventories are not an income-determining factor)	$ 816 26			
5. Less cost of operations (from Schedule D-2)	279 86			
6. Gross profit where inventories are not an income-determining factor (item 4 minus 5)		538 40		
7. Interest on loans, notes, mortgages, bonds, bank deposits, etc.		1,873 18		
8. Interest on obligations of the United States (from Schedule B, line 19 (a) (1))				
9. Rents		6,353 86		
10. Royalties		163,139 56		
11. Capital gain (or loss) (from Schedule E). (If a net loss, do not enter over $2,000)				
12. Dividends (from Schedule F)				
13. Other income (state nature of income) Miscellaneous		1 31		
14 Total income in Items 3, and 6 to 13, inclusive			$	173,906 31
DEDUCTIONS				
15. Compensation of officers (from Schedule G)		$		
16. Salaries and wages (not deducted elsewhere)		1,610 00		
17. Rent		600 00		
18. Repairs		4,518 05		
19. Bad debts (from Schedule H) See attached statement		14,160 00		
20. Interest		9,130 88		
21. Taxes (from Schedule D). (Do not include Federal excess-profits tax)		26,533 70		
22. Contributions or gifts (from Schedule J)				
23. Losses by fire, storm, etc. (Submit schedule, see Instruction 23)				
24. Depreciation (from Schedule K)		3,425 92		
25. Depletion of mines, oil and gas wells, timber, etc. (Submit schedule, see Instruction 25) 27 1/2%		44,863 38		
26. Other deductions authorized by law (from Schedule L)		14,963 24		
27. Total deductions in items 15 to 26, inclusive				119,805 17
28. Net income for excess-profits tax computation (item 14 minus item 27)			$	54,101 14
29 Less Federal excess-profits tax (see Instruction 29)		$ Exempt		
30. Interest on obligations of the United States (item 8, above)				
31. Net income for income tax computation (item 28 minus items 29 and 30)			$	54,101 14

Schedule B.—RECONCILIATION OF NET INCOME AND ANALYSIS OF EARNED SURPLUS AND UNDIVIDED PROFITS

1. Total distributions to stockholders charged to earned surplus during the taxable year	$	17. Earned surplus and undivided profits as shown by balance sheet at close of preceding taxable year (Schedule N)	$ 50,571 97
2. Contributions or gifts (excess over 5 percent limitation)		18. Net income for income tax computation (item 31, Schedule A	54,101 14
3. Federal income taxes	5,067 47	19. Nontaxable and partially exempt income:	
4. Income taxes of United States possessions or foreign countries if claimed as a credit in whole or in part in item 37, page 1 of return		(a) Interest on:	
5. Federal taxes paid on tax-free covenant bonds		(1) Obligations of a State, Territory, or political subdivision thereof, or the District of Columbia, or United States possessions	
6. Special improvement taxes tending to increase the value of the property assessed		(2) Obligations of United States issued on or before September 1, 1917, Treasury Notes, Treasury Bills, and Treasury Certificates of Indebtedness	
7. Replacements, renewals and capital expenditures charged to expenses on the books		(3) United States Savings Bonds and Treasury Bonds owned in the principal amount of $5,000 or less	
8. Insurance premiums paid on the life of any officer or employee where the corporation is directly or indirectly a beneficiary		(4) United States Savings Bonds and Treasury Bonds owned in the principal amount of over $5,000	
9. Unallowable interest incurred in purchasing or carrying exempt interest obligations		(5) Obligations of instrumentalities of the United States H.O.L.C. Bonds	79 06
10. Excess of capital loss, if any, over amount allowable as a deduction in item 11, Schedule A		(b) Other nontaxable income (itemize):	
11. Additions to surplus reserves (list each reserve separately):		(1) 1935 income tax refund	101 01
(a)		(2)	
(b)		(3)	
(c)		(4)	
(d)		20. Charges against surplus reserves deducted from income in the return (itemize):	
12. Other unallowable deductions:		(a) Depletion of oil	44,863 38
(a)		(b)	
(b)		(c)	
(c)		21. Adjustments for tax purposes not recorded on books (itemize):	
(d)		(a)	
13. Adjustments for tax purposes not recorded on books (itemize):		(b)	
(a)		(c)	
(b)		22. Sundry credits to earned surplus (itemize):	
(c)		(a) 1937 capital stock tax	
14. Sundry debits to earned surplus (itemize):		(b) reserve written off	250 00
(a) Adjustment of City and	9,316 65	(c)	
(b) county taxes - Per R.A.		(d)	
(c) R. Garbert's report			
(d)			
15. Earned surplus and undivided profits as shown by balance sheet at close of the taxable year (Schedule N)	34,442 50		
16. Total of lines 1 to 15	$ 48,826 62	23. Total of lines 17 to 22	$ 48,826 62

NOTE.—Attach to this return and mark as Schedule B-1, B-2, etc., analyses of surplus reserves, if any, as shown by the balance sheets (Schedule N), additions to which are not deductible for income and excess-profits tax purposes.

A-2

Schedule C

ANALYSIS OF PAID-IN OR CAPITAL SURPLUS

Page 3

1.	Debits to paid-in or capital surplus during the taxable year (to be detailed):	
	* * * * * * *	
2.	Paid-in or capital surplus as shown by balance sheet at close of the taxable year (Schedule N)	$371,872.13
3.	Total	$371,872.13
4.	Paid-in or capital surplus as shown by balance sheet at close of the preceding taxable year (Schedule N)	$371,872.13
5.	Credits during the year (to be detailed):	
	* * * * * * *	
6.	Total	$371,872.13

Schedule D-1

COST OF GOODS SOLD

(Where inventories are an income-determining factor)

[Not filled in]

Schedule D-2

COST OF OPERATIONS

(Where inventories are not an income-determining factor)

1.	Salaries and wages	$	
2.	Other costs (to be detailed):		
	(a) Cost of realized land sales	$	279.86
	* * * * * * *		
3.	Total (enter as item 5, Schedule A)	$	279.86

Schedule E

CAPITAL GAINS AND LOSSES

(From Sales or Exchanges Only)

[Not filled in]

Schedule F

INCOME FROM DIVIDENDS

[Not filled in]

Schedule G

COMPENSATION OF OFFICERS

(See Instruction 15)

[Not filled in]

Schedule H

BAD DEBTS (See Instruction 19)

* * * * * * *

4. Bad Debts Charged Off by Corporation if No Reserve Is Carried on Books

See attached statement ..... $ 14,160.00

[97]

Schedule I

TAXES

Page 4

Nature	Amount
Old Age Benefit—Payroll taxes	$ 16.10
Federal Production Tax—Crude Oil	49.73
California Oil & Gas Protection Fund	67.18
California Corporation Franchise Tax	1,419.07
Los Angeles City & County Taxes	24,981.62
Total (enter as item 21, Schedule A)	$26,533.70

Schedule J

CONTRIBUTIONS OR GIFTS

[Not filled in]

Schedule K.—DEPRECIATION

1. Kind of Property (If buildings, state material of which constructed)	2. Date Acquired	3. Cost or Other Basis	4. Assets Fully Depreciated in Use at End of Year	5. Depreciation allowed (or allowable) in Prior Years	6. Remaining Cost or Other Basis to Be Recovered	7. Life Used in Accumulating Depreciation	8. Estimated Remaining Life From Beginning of Year	9. Depreciation Allowable This Year
Office equipment	Var	$ 758.23	$	$ 304.66	$ 453.57	Var	Var	$ 73.00
Buildings—Stucco	Var	72,374.66		26,750.10	45,624.56	20	Var	3,352.92
Total (enter as item 24, Schedule A)								$3,425.92

Schedule L.—OTHER DEDUCTIONS (See Instruction 26)

Water expense	$ 262.72	Light maintenance	$ 241.88
Office expense	121.70	Trustee's fees	136.10
Wet oil expense	115.20	Commissions on house rentals	288.30
Insurance expense	309.43	Receiver's fees	7,315.15
Subdivision expense	9.12	Receiver's attorney's fees & expense	6,163.64

Schedule M

DISTRIBUTIONS TO STOCKHOLDERS AND DIVIDENDS PAID CREDIT

(See Instruction III)

[Not filled in]

[98]

ARTESIAN WATER COMPANY

Schedule M.—BALANCE SHEETS (See Instruction M)

	Beginning of Taxable Year		End of Taxable Year	
	Amount	Total	Amount	Total
ASSETS				
1. Cash		$ 21,962 17		$ 50,615 96
2. Notes receivable	$ 14,160 00		$	
3. Accounts receivable	13,684 10		16,616 82	
(a) Total of lines 2 and 3	$ 27,844 10		$ 16,616 82	
(b) Less reserve for bad debts		27,844 10		16,616 82
4. Inventories:				
(a) Raw materials	$		$	
(b) Work in process				
(c) Finished goods				
(d) Supplies				
5. Investments (Government obligations):				
(a) Obligations of a State, Territory, or political subdivision thereof, or the District of Columbia, or United States possessions	$		$	
(b) Obligations of the United States				
(c) Obligations of instrumentalities of the United States	2,875 00	2,875 00	2,875 00	2,875 00
6. Other investments:				
(a) Stocks of domestic corporations	$		$	
(b) Bonds of domestic corporations				
(c) Stocks and bonds of foreign corporations				
(d) Treasury stock				
(e) All other investments or loans				
7. Deferred charges:				
(a) Prepaid insurance, taxes, etc.		9,490 65		174 00
8. Capital assets:				
(a) Buildings	$		$	
(b) Machinery and equipment				
(c) Furniture and fixtures	701 58		758 23	
(d) Delivery equipment				
(e) Other depreciable assets				
(f) Total of lines (a) to (e)	$ 701 58		$ 758 23	
(g) Less reserve for depreciation	304 66	396 92	377 66	380 57
(h) Depletable assets	$		$	
(i) Less reserve for depletion				
(j) Land and buildings		1,002,371 86		999,618 94
9. Other assets (itemize below):				
Water rights	$ 1,000 00		$ 1,000 00	
Land sales contracts	94,357 49		91,308 55	
		95,357 49		92,308 55
10. Total Assets		$ 1,160,898 19		$ 1,162,789 84
LIABILITIES AND CAPITAL				
11. Accounts payable		$ 911 38		$ 318 13
12. Bonds, notes, and mortgages payable (with original maturity of less than 1 year)		185,464 78		100,250 00
13. Bonds, notes, and mortgages payable (with original maturity of 1 year or more)				
14. Accrued expenses:				
(a) Interest	$ 1,505 16		$ 940 61	
(b) Taxes	9,988 28		13,526 44	
(c) All others		11,493 44		14,467 05
15. Other liabilities (itemize below):				
Unrealized profit on land sales	$ 29,358 43		$ 28,820 03	
Contract deposits	150 00	29,508 43	400 00	29,220 03
16. Surplus reserves (itemize below):				
	$		$	
17. Capital stock:				
(a) Preferred stock	$		$	
(b) Common stock	612,220 00	612,220 00	612,220 00	612,220 00
18. Paid-in or capital surplus		371,672 13		371,672 13
19. Earned surplus and undivided profits		50,571 97		34,442 50
20. Total Liabilities and Capital		$ 1,160,898 19		$ 1,162,789 84

Schedule O.—CHANGES IN CORPORATION'S OBLIGATIONS AND CAPITAL STOCK (See Instruction O)

	Obligations	Preferred Stock*	Common Stock
1. Total cash receipts during taxable year from sale of corporation's own interest-bearing obligations with original maturity of 1 year or more and capital stock	$	$	$
2. Total cash expenditures during taxable year for purchase or retirement of corporation's own interest-bearing obligations with original maturity of 1 year or more and capital stock			
3. Difference between lines 1 and 2	$	$	$

*Preferred stock for this purpose should be considered as stock which is preferred as to either dividends or assets, irrespective of formal designation.

P—17M

AS

Schedule P.—NATURE OF BUSINESS Page 6

Check the block to indicate the industry in which the corporation's main income-producing business falls:

MANUFACTURING

Food and kindred products:
- ☐ Bakery and confectionery products.
- ☐ Canned products—fish, fruit, vegetables, etc.
- ☐ Mill products—bran, flour, feed.
- ☐ Packing-house products—meats, lard; slaughtering.
- ☐ Sugar—beet, cane, maple; molasses, etc.
- ☐ Other food products—butter substitutes, cereals, coffee, spices, dairy products; ice, etc.
- ☐ Beverages, soft drinks, mineral water.
- ☐ Brewing and distilling—alcohol, liquors, beer, malt extract, wines.
- ☐ Tobacco products.

Textiles:
- ☐ Cotton goods—dress goods, etc.; napping, dyeing.
- ☐ Woolen and worsted goods—dress goods, etc.; wool pulling, scouring.
- ☐ Silk and rayon goods—dress goods, thrown silk, etc.; spinning, warping.
- ☐ Carpets, floor coverings, tapestries, linoleum.
- ☐ Other textiles—cord, bit, fur, linen, artificial leather, surgical textiles, etc.
- ☐ Clothing—custom-made, factory-made; underwear, millinery, etc.
- ☐ Knit goods—sweaters, hosiery, etc.
- ☐ Leather boots, shoes, slippers, etc.

MANUFACTURING—(Cont.)
- ☐ Other leather products—saddlery, harness, trunks; furnishings, tanning.
- ☐ Rubber tires and tubes.
- ☐ Other rubber goods—boots, shoes, hose, surgical rubber.
- ☐ Soap, celluloid, and ivory products.
- ☐ Sawmills and planing mill products.
- ☐ Furniture (commercial).
- ☐ Other wood products—carriages, wagons, baskets, etc.
- ☐ Paper, pulp and products.
- ☐ Printing, publishing, and allied industries.
- ☐ Petroleum and other mineral oil refining and products.
- ☐ Chemicals proper, acids, compounds, coal-tar products, etc.
- ☐ Allied chemical substances, drugs, oils, soaps, etc.
- ☐ Paints, pigments, varnishes, etc.
- ☐ Fertilizers.
- ☐ Stones, clay, glass, and related products.

Metal products and processes:
- ☐ Iron and steel—products of blast furnaces, rolling mills, foundries.
- ☐ Locomotives and railroad equipment.
- ☐ Motor vehicles, complete or parts.

MANUFACTURING—(Cont.)

Metal products and processes—Continued.
- ☐ Machinery—heavy, used in producing food, textiles, steel, paper, rubber, glass, clay, stone, textile and wood products.
- ☐ Machinery—mechanical and equipment.
- ☐ Machinery—electrical and equipment.
- ☐ Machinery—other, building, construction, gas and mining machinery and equipment.
- ☐ Household equipment—metal furniture, refrigerators, sewing machines, etc.
- ☐ Office equipment.
- ☐ Metal building material and equipment.
- ☐ Hardware, tools, etc.
- ☐ Precious metal, products and processes.
- ☐ Other metals, products and processes.

Miscellaneous manufacturing:
- ☐ Radios, complete or parts.
- ☐ Musical, professional, and scientific instruments; optical goods, small boats.
- ☐ Airplanes, airships, engines; parts.

NONMANUFACTURING

Trades:
- ☐ Wholesale.
- ☐ Retail.

NONMANUFACTURING—(Cont.)
- ☐ Wholesale and retail.
- ☐ Commission.
- ☐ Other trade—agent, service, purpose, etc.

Finance:
- ☐ Banks—national, State, private, savings, commercial, trust, etc.
- ☐ Stock and bond brokers, investment houses or banks.
- ☒ Real estate, realty holding, and estate agents.
- ☐ Insurance companies (not agents).
- ☐ Investment trusts, stock syndicates, stock holding companies.
- ☐ Other finance—loan companies, building and loan associations, mortgage companies and brokers, and holding companies.

Miscellaneous and related industries, including hotels, laundry, barber, various holding and purchasing companies.
- ☐ Holding real estate, operating, buying and sell ing realty; realty and property.
- ☐ Communication—broadcasting, telegraph, telephone, cable, radio, short wave, television, and similar companies.
- ☐ Transportation—rail, water, air, bus, motor, etc.; trucking, also terminals.
- ☐ Power—gas and electric companies, utilities, and systems; steam, hydro, etc.
- ☐ Public utilities—electric light or power co. (privately or municipally owned), water, gas, steam, heat, refrigeration, ice, telephone, telegraph, bus and motor transportation, etc.
- ☐ Service—professional, business, amusement, domestic, and all other.

QUESTIONS

1. Date of incorporation April 23, 1900
2. State or country California
3. State collector's office where your return for the preceding year was filed 6th California
4. The corporation's books are in care of Wm. E. Ware, Receiver. Located at 727 West Seventh St. Los Angeles, Cal.
5. Is the corporation a personal holding company within the meaning of section 351 of the Revenue Act of 1936, as amended by the Revenue Act of 1937? Yes. If so, an additional return on Form 1120H must be filed.
6. Is this a consolidated return of railroad corporations? No. If so, procure from the collector of internal revenue for your district Form 851, Affiliations Schedule, which shall be filed in, sworn to, and filed as a part of this return.
7. If this is not a consolidated return of railroad corporations, and (a) you owned at any time during the taxable year 50 percent or more of the voting stock of another corporation either domestic or foreign or (b) any corporation, individual, partnership, trust or association, owned at any time during the taxable year 50 percent or more of your voting stock, attach separate schedule showing with respect to each: (1) name and address, (2) percentage of stock owned, (3) date stock was acquired, and (4) the collector's office in which the income tax return of such corporation, individual, partnership, trust, or association for the last taxable year was filed.
8. Was the income of this corporation included in a consolidated return for any prior year? No. If so, give name and address of corporation which filed the consolidated return and the last year for which such return was filed
9. Was the corporation in any way an outgrowth, result, continuation, or reorganization of a business or businesses in existence during this or any prior year since December 31, 1917? No. If answer is "yes", give name and address of each predecessor business, and the date of the change in entity

   Upon such change, were any asset values increased or decreased? If answer is "yes", closing balance sheets of the business and opening balance sheets of new business must be furnished unless furnished heretofore.
10. Is this return made on the basis of cash receipts and disbursements? No. If not, describe fully what other basis or method was used in computing net income Accrual
11. State whether the inventories at the beginning and end of the taxable year were valued at cost, or cost or market, whichever is lower. If other basis is used, describe fully, state why used, and the date inventory was last recomputed with
12. Did the corporation make a return of information on Form 1087, 1096, or 1099 (see Instruction I) for the calendar year 1937? No

AFFIDAVIT (See Instruction F)

William E. Ware, Receiver for

We, the undersigned, ~~president (or vice-president, or other principal officer) and treasurer (or assistant treasurer, or other principal officer)~~ of the corporation for which this return is made, being severally duly sworn, ~~each for himself~~ depose and say ~~that he is~~ (including any accompanying schedules and statements) has been examined by him and is, to the best of his knowledge and belief, true, correct, and complete return, made in good faith, for the taxable year stated, pursuant to the Revenue Act of 1936, as amended, and the Revenue Acts of 1936 and 1937, and the regulations issued thereunder.

Subscribed and sworn to before me this

14 day of March, 1938

William E. Ware, Receiver for (President or principal officer) (State title)

(Signature and title of officer administering oath)

Cashier, Wells Fargo (Treasurer, Assistant Treasurer, or Chief Accounting Officer) (State title)

My commission expires June 17, 1939

(If this return was prepared by some person or persons other than officers or employees of the corporation, the following affidavit must be executed)

AFFIDAVIT (See Instruction F)

I/we swear (or affirm) that I/we prepared this return for the person named herein and that the return (including any accompanying schedules and statements) is a true, correct, and complete statement of all the information respecting the income tax and/or excess profits tax liability of the person for whom this return has been prepared of which I/we have any knowledge.

Subscribed and sworn to before me this

_____ day of _____, 193__

_____ (Signature of person preparing the return)

_____ (Signature of person preparing the return)

_____ (Signature and title of officer administering oath)

_____ (Name of firm or employer, if any)

Artestian Water Company

Income Tax Return—Year 1937

Statement re: Exemption Claimed on Undistributed Profits Surtax:

Exemption from undistributed profits surtax is claimed on the following grounds. Attention is respectfully directed to Section 14 of the Revenue Act of 1936, part (d) (2) of which reads:

"(d) Exempt from surtax. The following corporations shall not be subject to the surtax imposed by this Section:

> "(2) Domestic corporations which for any portion of the taxable year are in bankruptcy under the laws of the United States, or are insolvent and in receivership in any Court of the United States, or of any State, Territory or the District of Columbia."

The word "insolvent" was apparently used in its dual sense by Congress. The Senate Finance Committee Report on the Revenue Bill of 1936 of June 1, 1936, on page 15, in discussing Section 14 (d) (2), said:

> "The Finance Committee Bill also avoids the possibility of tax avoidance by collusive receiverships by limiting the provision to cases in which the corporation is in bankruptcy under the Federal bankruptcy laws, and to cases in which it is insolvent, i.e., its liabilities are in excess of its assets or it is unable to pay the

> claims of creditors as they mature—and in receivership in Federal or State Courts."

The taxpayer was certainly unable to pay the claims of its creditors as they matured. That is, it was unable to pay them in the usual course of business out of quick assets without selling its capital assets. 32 Corpus Juris 806 states that the word "insolvency" has two meanings:

> "In its general and popular meaning, the term denotes the state of one whose entire property and assets, when converted into money without unreasonable haste or sacrifice, are insufficient to pay his debts; * * * But it is frequently used in the more restricted sense to express the inability of a person to pay his debts as they become due in the ordinary course of business."

Creditors claims, referred to above, which the corporation was unable to pay at maturity, consist of balance due the Pacific Mutual Life Insurance Company on account of money borrowed on November 12, 1929, and represented by two notes, one for $35,000 and one for $175,000. The note for $35,000 carried with it a specific agreement prohibiting the payment of dividends until said note was paid. During 1936 the sum of $26,750 was paid on this note leaving a balance of $8,250 which balance was paid during 1937, whereupon the note and collateral agreement were cancelled.

Similarly, during 1937 payments totaling $74,750 were made on the note for $175,000, making a grand total of payments made of $83,000.

The corporation owns subdivision land and oil producing property. The oil land is under lease to Shell Oil Company. The corporation secured its note to the Pacific Mutual Life Insurance Company by a mortgage on its properties, and gave as collateral security an assignment of the oil lease "together with all rents due, or to become due thereunder". The mortgagee notified Shell Oil Co. of the pledge of the lease and rents and instructed Shell Oil Co. to continue to pay the rents and royalties due under the lease to the corporation until further notice. The note and mortgage became due November 30, 1934, and is still past due. It has not been extended or renewed, and will outlaw November 30, 1938. [101]

The corporation has never been in a position to pay off the mortgage out of current assets. From the foregoing, it is apparent, therefore, the corporation was insolvent and in receivership during the taxable year 1937, and is exempt from the surtax under Section 14. [102]

Artesian Water Company
Year 1937

Supplemental Schedule—Item 19—Bad Debts:

Item of $14,160.00 represents note in principal amount of $12,000.00 plus interest accrued thereon to December 31, 1935, said interest having been re-

ported as income in 1933, 1934 and 1935, in the sum of $2,160.00 and was written off in 1937 as a bad debt. The following quotation is from letter of Meserve, Mumper, Hughes & Robertson, attorneys representing the receiver, relative to said note:

> "During the year 1937 we instituted the above entitled action for the purpose of collecting that certain promissory note dated December 13, 1934, in the amount of $12,000 with interest from January 1, 1932, until paid, at the rate of 6% per annum, payable semi-annually, in favor of Artesian Water Co. and signed by Maclay Rancho Water Co. by M. K. Rindge, President and P. D. Gowen, Secretary. We have been unable to effect any collection whatsoever on account of the judgment obtained in the above action. In fact, we have not even been able to recover costs expended in recovering the judgment. In our opinion, the judgment is, and at all times has been, valueless, and you are entitled to write off the note sued on as a loss for the year 1937."

A statement of the financial condition as of September 30, 1937 of the Maclay Rancho Water Co., prepared by its bookkeeper, disclosed the fact that, in the event of disposition at fair market values of its assets, it would not be possible to realize a sum sufficient to pay off the company's bonded indebtedness. [103]

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Rpt'd 6/12/38

UNITED STATES
1937 RETURN OF PERSONAL HOLDING COMPANY 1937

(Auditor's Stamp)

REVIEWED
SECTION II
J. M. WELLS
DATE MAR 8 1939

Treasury Department (Form 1120H) Internal Revenue Service

For Calendar Year 1937 or Fiscal Year

beginning ....., 1937, and ended ....., 1938

PRINT PLAINLY CORPORATION'S NAME AND ADDRESS

William E. Ware, Receiver for Artesian Water Co.
(Name)

727 West Seventh Street - Room 544
(Street and number)

Los Angeles (Post office) Los Angeles (County) California (State)

File Number 880267

District 6 - Calif.
(Cashier's Stamp)

Cash	Check	M. O.
	First Payment	
$		

Item and Instruction No. **ADJUSTED NET INCOME COMPUTATION UNDER TITLE IA (See Instruction I)**

1.	Net income (as defined in Title I of the Revenue Act of 1936, as amended by the Revenue Act of 1937)		$ 54,101 14
2.	Add: Contributions or gifts deducted in computing item 1 (see item 5 below)		
3.	Excess of expenses and depreciation over income from property not allowable under section 356 (b) (from Schedule A)		
4.	Total of items 1 to 3		$ 54,101 14
5.	Less: Contributions or gifts (from Schedule B) (not to exceed 15% of item 4)	$	
6.	Federal income, war-profits, and excess-profits taxes (from Schedule C)	5,027 33	
7.	Income and profits taxes of a foreign country or United States possession (not deducted in computing item 1)		
8.	Amount paid in liquidation of liability of the corporation based on liability of a decedent to make contributions or gifts (attach statement, see Instruction 8)		
9.	Total of items 5 to 8		5,027 33
10.	Adjusted net income (item 4 minus item 9)		$ 49,073 81

UNDISTRIBUTED ADJUSTED NET INCOME COMPUTATION (See Instruction J)

11.	Adjusted net income (item 10 above)		$ 49,073 81
12.	Less: Dividends paid credit	$	
13.	Amount used or irrevocably set aside to pay or retire indebtedness of any kind incurred prior to January 1, 1934 (from Schedule D, line 12)	83,000 00	
14.	Total of items 12 and 13		83,000 00
15.	Undistributed adjusted net income (item 11 minus item 14)		$ None

COMPUTATION OF TAX

16.	Surtax on portion of item 15, not in excess of $2,000, at 65%	$
17.	Surtax on amount of item 15, in excess of $2,000, at 75%	
18.	Total surtax in items 16 and 17	$ None

Furnish below the names and addresses of the individuals who owned, directly or indirectly, at any time during the last half of the taxable year, more than 50 percent in value of the outstanding capital stock of the corporation:

	Name	Address	Highest percentage of shares owned during last half of taxable year: Preferred	Common
(1)	Bank of America Nat'l Tr. & Savings	Assn-Pledgee for Frederick H. Rindge,	Los Angeles	1,533
(2)	Bank of America Nat'l Tr. & Savings	Assn-Pledgee for Mrs. May K. Rindge,	Los Angeles	1,277
(3)	Bank of America Nat'l Tr. & Savings	Assn-Pledgee for Mrs. Rhoda Rindge Adamson	"	844
(4)	Samuel K. Rindge	Los Angeles, California		844
(5)				

WILLIAM E WARE, RECEIVER FOR

AFFIDAVIT (See Instruction F)

We, the undersigned, ~~president (or vice president, or other principal officer) and treasurer (or assistant treasurer, or chief accounting officer) of~~ the corporation for which this return is made, being ~~severally~~ duly sworn, ~~each for himself~~ deposes and says that this return (including any accompanying schedules and statements) has been examined by him and is, to the best of his knowledge and belief, a true, correct, and complete return, made in good faith, for the taxable year stated, pursuant to the Revenue Acts of 1936 and 1937 and the Regulations issued thereunder.

Subscribed and sworn to before me this ..... day of ....., 193... William E Ware, Receiver for
(President or principal officer) (Name title)

CORPORATE SEAL

(Signature and title of officer administering oath) William Wells Company
(Treasurer, Assistant Treasurer, or Chief Accounting Officer) (Name title)

(If this return was prepared by some person or persons other than officers or employees of the corporation, the following affidavit must be executed)

AFFIDAVIT (See Instruction F)

I/we swear (or affirm) that I/we prepared this return for the person named herein and that the return (including any accompanying schedules and statements) is a true, correct, and complete statement of all the information respecting the surtax liability imposed by section 351 of the Revenue Act of 1936, as amended by the Revenue Act of 1937, of the person for whom this return has been prepared of which I/we have any knowledge.

Subscribed and sworn to before me this ..... day of ....., 193...

(Signature and title of officer administering oath)

(Signature of person preparing the return)

(Signature of person preparing the return)

(Name of firm or employer, if any)

NOTE.—One form marked "DUPLICATE COPY" must be filed with this original return ($10 will be assessed if duplicate copy is not filed)

9—17881

A-10

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Schedule A

EXCESS OF EXPENSES AND DEPRECIATION OVER INCOME FROM PROPERTY NOT DEDUCTIBLE UNDER SECTION 356

[Not filled in]

Schedule B

CONTRIBUTIONS OR GIFTS

[Not filled in]

Schedule C

FEDERAL INCOME, WAR-PROFITS, AND EXCESS-PROFITS TAXES

Nature of Tax	Taxable Year	Amount
Federal Income Tax—Normal	1936	$4,145.91
Federal Excess Profits	1936	617.82
Federal Surtax on Und. Profits	1936	263.60
Total (enter as item 6, first page)		$5,027.33

Schedule D

AMOUNTS USED OR SET ASIDE TO PAY OR RETIRE INDEBTEDNESS INCURRED PRIOR TO JANUARY 1, 1934

	I
1. Description of indebtedness	Mortgage Note
2. Date incurred or assumed	November 12, 1929
3. Date due	November 30, 1934
4. Original amount of indebtedness	$210,000.00
5. Amount used or set aside prior to January 1, 1934, to pay or retire such indebtedness	
6. Excess of indebtedness on January 1, 1934, over total amount used or set aside prior to that date to pay or retire such indebtedness	$210,000.00

7. Amounts used or set aside to retire such indebtedness during the following calendar years, or during fiscal years beginning in such calendar years

1934	$
1935	
1936	26,750.00

8. Amount used or irrevocably set aside during the taxable year covered by this return to pay or retire such indebtedness 83,000.00

9. Total of lines 7 and 8 ..... $109,750.00

10. Balance of indebtedness (line 6 minus line 9) $100,250.00

11. Indicate separately:

(a) Amount actually used during the taxable year covered by this return to pay or retire the indebtedness ..... $ 83,000.00

(b) Amount irrevocably set aside during the taxable year covered by this return to pay or retire the indebtedness, but not actually used during the taxable year for such purpose ..... $

12. Portions of amounts entered on line 8 above, claimed as deductions for the taxable year covered by this return (enter total as item 13, first page) ..... $ 83,000.00

Indicate by check mark whether the deduction claimed in item 13, first page of this return, represents:

A ☒ Amount actually used during the taxable year to pay or retire the indebtedness;

B ☐ Amount irrevocably set aside during the taxable year to pay or retire the indebtedness; or

C ☐ Combination of both A and B.

There must be furnished all of the facts and circumstances upon which the taxpayer relies to establish the reasonableness of the amount claimed as a deduction. Describe fully

the plan for payment or retirement of the obligations, indicating date and method of adoption, and where the plan is covered by a mandatory sinking fund agreement or similar arrangement, submit a copy of the indenture or agreement by which the fund was established and under which it is maintained—See attached statement.

If the amount claimed as a deduction in item 13, first page of this return, represents an amount irrevocably set aside to pay or retire the indebtedness, explain fully the circumstances and method by which it was irrevocably set aside.

[105]

Artesian Water Company
Personal Holding Company Return
Year 1937

Statement re: Item 13 (from Schedule D)
Amounts Used to Pay Indebtedness Incurred Prior to January 1, 1934:

The indebtedness consists of note secured by mortgage given to Pacific Mutual Life Insurance Co. The note and mortgage became due November 30, 1934 and is still past due. It has not been extended or renewed and will outlaw November 30, 1938. The mortgage includes oil land under lease to Shell Oil Company and other acreage and is further secured by the assignment of existing leases which constitute the corporation's chief source of income. The mortgagee notified Shell Oil Co. of the pledge of the lease and rents, and instructed the Shell Oil Co. to continue to pay the rents and royalties due under the lease to the corporation until further notice.

As a result of numerous discussions with the mortgagee relative to the payment of the indebtedness the receiver tendered to the mortgagee and the mortgagee accepted payments of $2,750 per month on the principal, in addition thereto sums totaling $50,000.00 were paid and accepted during 1937. This procedure followed an expressed intention of the mortgagee to collect from the lessee the royalties from the oil lease, or to foreclose. The payments on principal during 1937 totaled $83,000.00, and same were made with the approval and by authorization of the Superior Court of the State of California, which has jurisdiction over the corporation's receivership.

The mortgagee has formally refused to extend or renew the mortgage. At the present time the indebtedness is past due and subject to possible action by the mortgagee. The mortgage cannot be refinanced while the corporation is in receivership, as no one will take a note or mortgage signed by the receiver.

The payment of $83,000.00 in 1937 was reasonable, considering the size and terms of the mortgage, and considering also that the oil royalties were pledged to the mortgagee, and that the pledgee was entitled to take the royalties to apply on interest and principal (Section 2989 of the California Civil Code, 21 Cal. Jur. 312, 14 C. J. 822). Consideration should also be given to the fact that the corporation was in receivership and the court authorized these payments. [106]

1937 RETURN OF CAPITAL-STOCK TAX
For Year Ending June 30, 1937

Domestic Corporations
(Sec. 105, Revenue Act of 1935, as amended by Sec. 401 of the Revenue Act of 1936)

This return must be filed, in triplicate, and received by the Collector of Internal Revenue for your district on or before July 31, 1937. The tax must be paid on or before that date.

1. Name—William E. Ware, Receiver for Artesian Water Company.

2. Address—727 West Seventh Street, Los Angeles, California.

3. Name of parent company, if any..... (District filed .....)

4. Name of subsidiary, if any..... No. shares held..... (District filed .....)

5. Nature of business in detail—Land Owners.

6. Incorporated or organized in State of California. Month April Day 23rd Year 1900.

7. Was a capital-stock tax return filed for the preceding taxable year ended June 30, 1936? Yes. If filed under a different name, state the name..... (District filed .....)

8. Date of close of last income-tax taxable year ended on or prior to June 30, 1937, or, if newly organized corporation having no income-tax taxable year ended on or prior to June 30, 1937, date of organization.....

Corporation making an original declaration of value upon this return must enter the amount of such declared value in item 9. This block is not to be used by a corporation which established its original declared value by the first return for the year ended June 30, 1936.

9. Original declared value of entire capital stock.....$.....

(The value declared must be definite and unqualified. A value must be declared in every case regardless of whether exemption from the tax is claimed. See instructions 1 and 3)

Corporations which have established their original declared value by the return for the year ended June 30, 1936, must adjust such declared value as provided for in Schedule I on page 2 of this return and then after the amount of the adjusted declared value in item 10.

10. Adjusted declared value of entire capital stock (Last item of Schedule I, page 2)...$310,944.44

11. Exemptions.—The Act provides for an exemption from the tax only on the grounds indicated below. Corporations claiming exemption must (1) report a value for the capital stock under item 9 or 10, (2) check the appropriate block below, showing the basis of the claim, and (3) submit with the return a full statement of the evidence specified under the block checked.

☐ Corporation exempt from income tax under section 101, Revenue Act of 1936. (1) State under which subsection of section 101 ..... (2) Furnish information required by instruction 14.

☐ Insurance company subject to tax under section 201, 204, or 207, Revenue Act of 1936. State which section.....

☐ Corporation not doing business. (1) Furnish information required by instruction 16. (2) Report value of capital stock in item 9 or 10 above.

Computation of Tax	For Use of Taxpayer	For Use of Department
12. Amount reported in item 9 or 10	$310,944.44	$.....
13. Tax at rate of $1 for each full $1,000 in item 12 (omit cents)	Exempt	xxxx
14. Penalty of ..... percent for delinquency in filing return	.....	.....
15. Interest at 6% per annum beginning August 1, 1937	.....	.....
16. Total tax, penalty, and interest	.....	.....

I, the undersigned William E. Ware, Receiver for Artesian Water Co. and ....., ..., of the corporation for which this return is made, being severally duly sworn, each for himself deposes and says that this return, including any accompanying schedules and statements, has been examined by him and is, to the best of his knowledge and belief, a true and complete return, made in good faith, for the taxable year stated, pursuant to the Revenue Act of 1935, as amended, and the Regulations issued thereunder.

Sworn to and subscribed before me this.....day of ....., 193.....

[Corporate Seal] WILLIAM E. WARE
Receiver

[Notarial Seal] .....

.....

[Exemption allowed. Jan. 8, 1938. JMB]

[107]

Page 4

The schedules on this page must be filled in by every corporation making adjustments to an original declared value for the capital stock established by the return for the year ended June 30, 1936. See instructions 5 to 9, inclusive.

SCHEDULE I. ADJUSTMENT OF ORIGINAL DECLARED VALUE OF ENTIRE CAPITAL STOCK FOR ALL TRANSACTIONS DURING THE INCOME-TAX TAXABLE YEAR ENDED DECEMBER 31, 1936.

Original declared value as established by the first return for the taxable year ended June 30, 1936..... $250,000.00

Additions:

(1) (a)	Total cash paid in for stock or shares (see instruction 7, item 1)..... $	—
(b)	Fair market value of all property received for stock or shares (see instruction 7, item 1).....	—
(2)	Paid-in surplus and contributions to capital (see instruction 7, item 2).....	—
(3)	Net income (see instruction 7, item 3)	34,679.23
(4)	Excess of income wholly exempt from tax over amount disallowed as deductions by section 24 (a) (5) of the Revenue Act of 1934 or 1936 (see instruction 7, item 4).....	26,265.21

(5) Dividend deduction allowable for income-tax purposes (see instruction 7, item 5)	—	
Total additions		60,944.44
Total Before Deductions		$

Deductions:

(A) (1) Total cash distributed in liquidation to shareholders (see instruction 7, item A)	$ —	
(2) Fair market value of all property distributed in liquidation to shareholders (see instruction 7, item A)	—	
(B) Distributions of earnings or profits (see instruction 7, item B)	—	
(C) Excess of deductions allowable over gross income and claimed on income-tax return (see instruction 7, item C)	—	
Total deductions		—
Adjusted Declared Value (enter in item 10, page 1)		$310,944.44

SCHEDULE II. ANALYSIS OF CHANGES IN CAPITAL STOCK AND SURPLUS

Capital Stock and Surplus at beginning of year

1. Capital stock: Preferred		
Common	$612,220.00	
2. Capital or paid-in surplus		
3. Surplus reserves		
4. Surplus and undivided profits	264,431.87	

Additions—Capital transactions

5. Total cash and fair market value of property paid in for stock or shares (total of items 1(a) and 1(b), Schedule I)*		

6. Paid-in surplus and contributions to capital (item 2, Schedule I)*	
7. Other additions (to be detailed)	
Additions—Revenue transactions	
8. Net income (item 3, Schedule I)	34,679.23
9. Income wholly exempt from income tax. (This total less the amount entered as item 17 of this schedule should correspond with item 4, Schedule I) (See instruction 7, item 4)	26,265.21
10. The amount of the dividend deduction allowable for income-tax purposes (item 5, Schedule I) (see instruction 7, item 5)	
11. Other additions (to be detailed)	
Sign space rental (1934-5)	146.63
1936 Excess Profits tax	617.82
Total	$938,360.76
Deductions—Capital transactions	
12. Liquidating distributions (total of items A(1) and A(2), Schedule I)*	
13. Other distributions (item B, Schedule I)*	
14. Enter class and amount of distributions in corporation's own stock:	
$	x x x x x
15. Other deductions (to be detailed)	
Deductions—Revenue transactions	
16. Excess of deductions allowable over gross income and claimed on income-tax return (item C, Schedule I)	
17. Deductions disallowed by sec. 24(a)(5), 1934 or 1936 Act. (See item 9 of this schedule)	
18. Other deductions (to be detailed)	
Taxes paid (for prior yrs)	4,149.34
Street bonds (for prior yrs)	76.74
1935 Income tax	614.52

Capital Stock and Surplus at end of year

19. Capital stock: Preferred		
	Common	612,220.00
20. Capital or paid-in surplus		
21. Surplus reserves		
22. Surplus and undivided profits		321,300.16
Total		$938,360.76

*Enter values shown by the books if different from values entered in Schedule I and explain difference.

[108]

Mr. Tonjes: With permission to withdraw the original and substitute a photostat.

The Member: Yes. Permission will be granted to substitute a photostat.

The Clerk: Let the record show that counsel for the respondent is withdrawing Petitioner's Exhibit No. 9, the income tax return, for the purpose of making a photostatic copy.

The Member: Do you desire that the time for the filing of briefs be fixed at forty-five days as provided by the rules, or do you wish a different time?

Mr. Witter: That time is satisfactory to me.

Mr. Tonjes: I believe that will be satisfactory.

If Your Honor please, I am wondering in view of the fact that Mr. Witter desires to point out some of the local law and its applicability, whether it might not be more helpful to have Mr. Witter file an opening brief and I will file a reply brief, giving

him of course the opportunity to reply if he cares to. [74]

The Member: If you desire to do it that way the Board has no objection.

That would be July 26th for the filing of Petitioner's brief. And you would like thirty days thereafter in which to file a reply brief, Mr. Tonjes?

Mr. Tonjes: Yes, Your Honor.

The Member: Which would be August 26th.

And then if Petitioner desires to file a reply to your brief he may have until September 10th in which to file the reply brief.

Mr. Witter: That is satisfactory.

Mr. Tonjes: That is satisfactory.

The Member: The hearing is concluded.

(Hearing concluded)

[Endorsed]: U. S. B. T. A. Filed July 11, 1940. [75]

In the United States Circuit Court of Appeals for the Ninth Circuit

[Title of Cause.]

PRAECIPE

To the Clerk of the United States Board of Tax Appeals:

You will please prepare and within the time allowed by law transmit to the Clerk of the United States Circuit Court of Appeals for the Ninth Cir-

cuit certified copies of the following documents:

(1) Documentary entries of proceeding before the United States Board of Tax Appeals in the above-entitled cause;

(2) Pleadings before the Board in said cause.

(a) Petition.

(b) Amended Petition.

(c) Answers.

(3) Complete Transcript of Proceedings and Testimony at hearing together with Exhibits introduced.

(4) Findings of Fact, opinion and decision of the Board. [109]

(5) Petition for Review by the United States Circuit Court of Appeals for the Ninth Circuit;

(6) Notice of filing said Petition for Review;

(7) This Praecipe.

The foregoing to be prepared, certified and transmitted as required by law and the rules of the United *States Court* of Appeals for the Ninth Circuit.

GEORGE G. WITTER
Attorney for Petitioner

[Endorsed]: U. S. B. T. A. Filed Apr. 16, 1941. [110]

[Title of Board and Cause.]

CERTIFICATE

I, B. D. Gamble, Clerk of the U. S. Board of Tax Appeals, do hereby certify that the foregoing pages, 1 to 110, inclusive, contain and are a true copy of the transcript of record, papers, and proceedings on file and of record in my office as called for by the Praecipe in the appeal (or appeals) as above numbered and entitled.

In testimony whereof, I hereunto set my hand and affix the seal of the United States Board of Tax Appeals, at Washington, in the District of Columbia, this 1st day of May, 1941.

[Seal] B. D. GAMBLE,
Clerk,
United States Board of Tax Appeals.

[Endorsed]: No. 9824. United States Circuit Court of Appeals for the Ninth Circuit. Artesian Water Company, a corporation, Petitioner, vs. Commissioner of Internal Revenue, Respondent. Transcript of the Record. Upon Petition to Review a Decision of the United States Board of Tax Appeals.

Filed May 16, 1941.

PAUL P. O'BRIEN,
Clerk of the United States Circuit Court of Appeals for the Ninth Circuit.

In the United States Circuit Court of Appeals
for the Ninth Circuit

U. S. C. C. A. No. 9824

Docket No. 100824

ARTESIAN WATER COMPANY, a corporation,
Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

To the Clerk of the Circuit Court of Appeals:

Petitioner hereby assigns the following errors and designates the entire record for printing:

ASSIGNMENT OF ERRORS ON APPEAL

(1) The Board erred in holding that the Petitioner was subject to surtax under Section 14 of the Revenue Act of 1936 for not distributing its profits in the year 1937.

(2) The Board erred in not finding as a fact, and holding as a matter of law, that the Petitioner was in receivership and insolvent during 1937, or a portion thereof, and, therefore, under the provisions of Section 14 (d)(2) of the Revenue Act of 1936, not subject to surtax imposed by Section 14 (b) of that Act.

(3) The Board erred in not finding as a fact, and holding as a matter of law, that the mortgages of Petitioner's income producing assets and the assignment of its leases, under the circumstances and commitments existing in the taxable year, did con-

stitute a contract restricting it from the payment of dividends within the meaning of Section 26 (c)(1) of the Revenue Act of 1936.

(4) The Board erred in not finding as a fact, and holding as a matter of law, that the mortgages of Petitioner's income producing assets and assignment of Petitioner's leases, under the circumstances and commitments existing in the taxable year, did constitute a requirement that the Petitioner pay on, or set aside for payment on, its indebtedness, its earnings and profits of the taxable year and, therefore, rendering it exempt from surtax under the specific provisions of Section 14 (c)(2) of the Revenue Act of 1936.

(5) The Board erred in holding that the Statutes of California prohibiting Petitioner from declaring a dividend while it was unable to pay its debts, did not constitute a contract exempting the Petitioner from surtax on undistributed profits under the provisions of Section 26 (c)(1) and (2) of the Revenue Act of 1936.

DESIGNATION OF PORTIONS OF THE RECORD

The Petitioner desires that the entire certified transcript be printed for the record on appeal.

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[Endorsed]: Filed May 21, 1941. Paul P. O'Brien, Clerk.

No. 9824.

IN THE

United States Circuit Court of Appeals

FOR THE NINTH CIRCUIT

ARTESIAN WATER COMPANY, a corporation,

Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,

Respondent.

BRIEF FOR APPELLANT.

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BRIEF FOR APPELLANT.

Statement of Pleadings and Jurisdiction.

The Commissioner of Internal Revenue issued to the petitioner a letter dated September 21, 1939, alleging a deficiency in income tax for the calendar year 1937, and allowing the petitioner ninety days within which to appeal to the United States Board of Tax Appeals [Tr. p. 7].

On December 12, 1939, the petitioner filed its appeal with the United States Board of Tax Appeals [Tr. p. 3]. The respondent's answer thereto was filed on January 23, 1940 [Tr. p. 12].

The appeal was heard before a member of the Board of Tax Appeals, sitting at Los Angeles, California, on

June 11, 1940. On January 22, 1941, the Board handed down its findings of fact and opinion and entered its final order in the appeal [Tr. pp. 21-37].

On April 16, 1940, the petitioner filed its petition for review by the United States Circuit Court of Appeals (Ninth Circuit) [Tr. p. 38], and duly completed the filing of said petition by service of a copy thereof and a praecipe upon counsel for the respondent [Tr. p. 132], proof of which service is on file with the clerk of this Honorable Court.

Statement of the Case.

The only question in this case is whether the petitioner should be subjected to the undistributed profits tax (Revenue Act of 1936, Section 14) for not having distributed its income to its stockholders in the calendar year 1937.

Briefly stated, the facts are:

The petitioner, a California corporation, was an owner of lands. In 1929 it gave its note for $175,000.00 to the Pacific Mutual Life Insurance Company to cover indebtedness owed to that company. It secured this note by a mortgage on all its income-producing assets [Tr. p. 77] and, as additional security, petitioner assigned to the insurance company its lease with Shell Oil Company and all the income therefrom [Tr. p. 24]. The latter income from oil constituted over 90 per cent of petitioner's total income [Tr. p. 24]. In 1931 petitioner gave the insurance company an additional note for $35,000.00, which note was not subjected to the prior mortgage and assignment, but, with respect to this note, the petitioner agreed not to declare dividends until it was paid.

Both of these notes matured on November 12, 1934. Nothing was paid on the principal of either note at maturity. Petitioner requested extension of time, but was refused [Tr. p. 84].

In 1935 the petitioner was placed in involuntary receivership, not by its own creditors but by a creditor of one of its stockholders. The receivership continued until 1939, when petitioner was discharged.

As soon as appointed the receiver started negotiations with the insurance company for an extension of time within which to pay the two notes above mentioned. After several refusals, the receiver was finally given an informal extension to March 3, 1937, provided certain payments were made each month in the interim. The receiver was notified in writing at this time, however, that no extension would be granted beyond March 2, 1941, and that the insurance company would expect payment to be made in full not later than that date. The receiver made strenuous and determined efforts to refinance the notes. He negotiated with many banks and brokers, but without success.

Unable to refinance, the receiver paid such amounts as he could. In 1936 he paid $26,750.00, all of which was applied on the second note. In 1937 the receiver paid a total of $83,000.00, $8,250.00 of which paid the balance owing on the second note, and the remainder, or $74,-750.00, was applied on the first note. Every payment was made pursuant to the instruction and order of the Superior Court. In the taxable year 1937 petitioner paid its entire net income on the notes, plus approximately $30,000.00 out of its depletion reserves. At the close

of the taxable year petitioner still owed a balance of $100,250.00, which, at the time, it was wholly unable to pay.

The petitioner filed its income tax return for 1937 and paid a normal income tax of $6,955.17. The Commissioner found the income stated in the return correct and the normal tax paid correct, but imposed on the petitioner a surtax of $7,380.33 for not having distributed its income to its stockholders. In asserting such surtax, under Section 14 of the Revenue Act of 1936, Commissioner allowed as a credit the $8,250.00 paid in 1937 on the second note, but refused to allow any credit for amounts paid on the first note.

Assignment of Errors.

(1) The Board erred in holding that the petitioner was subject to surtax under Section 14 of the Revenue Act of 1936 for not distributing its profits to its stockholders in the year 1937.

(2) The Board erred in not finding as a fact, and holding as a matter of law, that the petitioner was in receivership and insolvent during 1937, or a portion thereof, and, therefore, under the provisions of Section 14(d)(2) of the Revenue Oct of 1936, not subject to surtax imposed by Section 14(b) of that Act.

(3) The Board erred in not finding as a fact, and holding as a matter of law, that the mortgages of petitioner's income producing assets and the assignment of its leases and income, under the circumstances and commitments existing in the taxable year, did constitute a contract restricting it from the payment of dividends within the meaning of Section 26(c)(1) of the Revenue Act of 1936.

(4) The Board erred in not finding as a fact, and holding as a matter of law, that the mortgages of petitioner's income producing assets and assignment of petitioner's leases and income, under the circumstances and commitments existing in the taxable year, did constitute a requirement that the petitioner pay on, or set aside for payment on, its indebtedness, its earnings and profits of the taxable year and, therefore, render it exempt from surtax under the specific provisions of Section 14 (c) (2) of the Revenue Act of 1936 to the extent such earnings were so applied.

Summary of Argument.

The petitioner was in receivership and insolvent in the year 1937 and therefore, under Section 14(d)(2), not subject to undistributed profits tax. By the word "insolvent", Congress meant "unable to pay the claims of creditors as they mature."

Long prior to the taxable year the petitioner had assigned its oil lease and all income therefrom to its creditor, the Pacific Mutual Life Insurance Company. Such assignment under California laws, which is controlling, passes full title in such income to the creditor. Income so assigned was no longer available to the petitioner for the declaration of dividends. Such assignment constitutes a contract, expressly restricting the payment of dividends and expressly making disposition of the earnings and profits within the meaning of Section 26(c)(1) and (2) of the Revenue Act of 1936. As petitioner's entire income was applied in partial payment of its debt, it is entitled to credit against undistributed profits tax for the entire amount of the same under Section 26(c)(1) and (2).

ARGUMENT.

I.

The Petitioner Was in Receivership and Insolvent in the Taxable Year.

Section 14(d)(2) of the Revenue Act of 1936 provides as follows:

> "(d) EXEMPTION FROM SURTAX.—The following corporations shall not be subject to the surtax imposed by this section:
>
> * * * * * * * *
>
> "(2) Domestic corporations which for any portion of the taxable year are in bankruptcy under the laws of the United States, or are insolvent and in receivership in any court of the United States or of any State, Territory, or the District of Columbia.
>
> * * * * * * * *"

There is no question about the receivership, so we pass to the question of insolvency.

The word "insolvent" is a flexible term that has been given various meanings, sometimes by statute, and often by the courts in varying situations. I have no doubt if the word "insolvent" had merely been inserted in Section 14(d)(2) and no definition left by Congress, that the courts, with an eye to the essential nature of the undistributed profits tax and its potential harshness in operation, would have given the term its most liberal meaning. But conscious perhaps of the several meanings attached to the word "insolvent", the Senate Finance Committee, who inserted the word into the Act, also defined the meaning it was to carry. The following is an extract from the report of the Senate Finance Committee on the Revenue Bill of 1936, found on page 15 of that report, dated

June 1, 1936. In discussing Section 14(d)(2), the chairman said:

> "Section 105 of the House Bill exempted domestic corporations in bankruptcy or receivership from the undistributed-profits tax in that bill and subjected them to a flat 15 per cent rate of tax. The bill as reported (section 14(c)(2)) similarly exempts such corporations from the 7 per cent undistributed-profits surtax and applies to them the graduated rates applicable to other corporations. The committee proposal specifically exempts the corporation in this situation from the undistributed-profit surtax for its entire taxable year even if it is bankrupt or in receivership for only a part of the taxable year. This proposal is founded on the principle that if a corporation goes into bankruptcy or receivership after its taxable year has started, it is so weak that an undistributed-profits surtax ought not to be or can not be imposed upon it. Similarly, if it comes out of bankruptcy or receivership during its taxable year, it should be allowed to operate free of such tax during the remainder of the year in order to recover its strength. The Finance Committee bill also avoids the possibility of tax avoidance by collusive receiverships by limiting the provision to cases in which the corporation is in bankruptcy under the Federal bankruptcy laws, and to cases in which it is insolvent—i. e., its liabilities are in excess of its assets or it is unable to pay the claims of creditors as they mature—and in receivership in Federal or State courts."

The report, we believe, evidences three things:

(1) That the word "insolvent" was added to prevent collusive receiverships instigated to evade tax. There is no question of collusion here because the receivership was

instituted in 1935, before an undistributed profits tax was even discussed.

(2) That Congress recognized the potential harshness of the tax and sought to safeguard a company in a weakened financial condition against its operation.

(3) That the word "insolvent" means a taxpayer unable to pay its debts as they mature.

The Government argued below that the statute intends that the receivership shall be instituted *on the ground of* insolvency. If the Board did not actually acquiesce in this position, it, at least, emphasized it greatly in its opinion. We find no such requirement in the statute. The statute merely requires that the two conditions be concurrent, that is, that the taxpayer be *in receivership* and *insolvent* at the same time and at sometime during the taxable year. A taxpayer who is laboring under those two conditions is in just as bad a position, regardless of how he was placed into receivership. All of the reasoning that urges the relief from the tax in the case of one, urges it in the case of the other. We see no ground for the distinction either in the wording of the statute, or outside the statute.

The evidence in this case shows beyond any reasonable doubt that this petitioner was unable to pay its matured and past due debts in the year 1937. It is the petitioner's contention that when this is shown, it matters not if its assets under normal conditions were in excess of its liabilities (see cases cited below on this point), and it matters not if its inability to pay its debts was due in part, or in whole, to the fact that it was in receivership. The solvency or insolvency of the petitioner, that is, its ability to pay its debts, must be determined in the actual situation in which the petition is found in the taxable year and

not in some false and assumed situation in which it is not found, for example, free from receivership.

Passing to a review of the evidence and findings, we find the following:

(1) Immediately upon his appointment, the receiver began negotiations to obtain an extension of the loans. [Board's Findings of Fact, Tr. p. 26.]

(2) The conservator appointed for the Pacific Mutual Life Insurance Company in 1936 disapproved the loans and refused any extension of time. [Board's Findings of Fact, Tr. p. 27.]

(3) The receiver then attempted to refinance the loans but was unsuccessful. [Board's Findings of Fact, Tr. p. 26.]

(4) In his efforts to refinance the loans the receiver negotiated with the loaning officers of the California Bank, Security-First National Trust & Savings Bank, and two or three other banks in town, with the idea of attempting to procure a new loan. All of the negotiations fell through, due to the fact that none of the loaning officers felt they could make a new loan signed by the receiver. The title companies would not issue satisfactory title. [Rec's Test, Tr. p. 97.] The negotiations failed, also, because the value of the properties was more or less unknown. The Security Bank spent considerable time in appraising the properties but declined the loan. [Rec's Test, Tr. p. 98.] The receiver's efforts to refinance were also hampered and embarrassed because of the fact that the notes were already two years in default. That objection was brought up continually. [Rec's Test, Tr. p. 104.]

The receiver's testimony and the Board's findings show without any doubt that in 1937 this petitioner was in a

spot where it could not pay its debts. The receiver made every effort to do so, even to pledging and hypothecating all of the assets of petitioner and assigning all of its income, but without success.

One of the most frequently applied rules in determining insolvency is whether or not a company or individual is able to pay its debts in the *ordinary course of business.*

Cincinnati Equipment Co. v. Degnan, 184 Fed. 834:

> " 'Insolvency' as counsel urge it, is statutory, and in administering the bankruptcy act must be strictly adhered to. * * * Insolvency has, however, another and different meaning. To illustrate, we may refer to the definition given by the Supreme Court when considering the term 'insolvency' under the bankruptcy act of 1867, which did not define the term. As stated by Justice Clifford in *Dutcher v. Wright,* 94 U. S. 553, 24 L. Ed. 130:
>
> " 'Insolvency,' in the sense of the bankrupt act, means that the party whose business affairs are in question is unable to pay his debts as they become due, in the ordinary course of his daily transactions. *Wagner v. Hall,* 16 Wall. 584, 599, 21 L. Ed. 504. *Toof v. Martin,* 13 Wall. 40, 47, 20 L. Ed. 481.
>
> "Insolvency was many years ago defined in Ohio to be (*Mitchell v. Gazzam,* 12 Ohio, 315, 336):
>
> " '* * * But, in the broad sense used by the staute, it means a person whose affairs have become so deranged that he is unable to pay his debts as they fall due * * *.'
>
> "In *American Can Co. v. Erie Preserving Co.* (C. C.) 171 Fed. 540, 542, it is said:
>
> " 'The allegations in the bill that the defendant could not pay its current obligations as they matured,

and that it was unable in the ordinary course of its business to pay its existing and enforceable liabilities, was a proper and sufficient allegation of insolvency * * *. Insolvency as the term is used in equity, is clearly differentiated from the meaning which is given it by bankruptcy act.'"

Bull v. International Power Co., 84 N. J. Eq. 6; 92 A. 796:

"The corporation was insolvent although it had a large balance of assets over and above its liabilities, where it appeared that it had not sufficient money on hand to meet the taxes due the state, salaries of officers and the administrative expenses of employers, and although the president of the company declared that he could coerce another company to declare a dividend which would be sufficient to put cash capital into the treasury and meet its current obligations."

Fieldmeier v. Mortgage Securities, Inc., 34 Cal. App. (2d) 201, at 244:

"It is beyond dispute that the company was, is and for some time prior to September 1931, *insolvent* in the sense of being unable to pay its debts as they became payable. * * * Even if it had non-liquid assets that at a fair valuation ought to have largely exceeded its liabilities, it had no assurance that it would not be required to sacrifice them for a small part of their nominal value."

Sam Ramazzina et al., Co-partners Under the Firm Name and Style of Ramazzina Brothers, an Insolvent Debtor, 110 Cal. 488;

Dixon Lumber Co. v. Peacock, 217 Cal. 415, 421;

Southwich v. Moore, 61 Cal. App. 585, 589;

Russell etc. Co. v. E. C. Faitonta Hdw. Co. (N. J. Ch.), 62 Atl. 421;

Baker v. Emerson, 4 App. Div. 348, 38 N. Y. 5576;

Thompson v. Thompson, 4 Cush. (Mass.) 127, 134.

Section 3450, Civil Code of California:

"A debtor is insolvent, within the meaning of this title, when he is unable to pay his debts from his own means as they become due."

Sam Ramazzina et al., Co-partners Under the Firm Name and Style of Ramazzina Brothers, an Insolvent Debtor, 110 Cal. 488:

"* * *

"It is also insisted that the co-partnership of Ramazzina Brothers was not insolvent at the time of the filing of said petition, as shown by a comparison of its assets and liabilities appearing therein. While it does appear therefrom that the valuation of the partnership assets exceeds considerably the liabilities of the partnership, yet the petition further discloses that the partners individually are hopelessly insolvent. The petitioners further allege directly that they are insolvent, and the mere fact that the assets in value exceed their liabilities does not prove solvency. Such fact might exist, and often does exist, and still a debtor be entirely insolvent within the purview of the Insolvent Act. * * *."

First National Bank of Silverton v. E. J. Walton, 5 L. R. A. 765, Colorado Supreme Court:

"By insolvency is meant an inability to fulfill one's obligations according to his undertaking, and general

> inability to answer in court for all of one's liabilities existing and capable of being enforced; not an absolute inability to pay at some future time, upon a settlement and ending up of a trade, but as not being in condition to pay one's debts in the ordinary course, as persons carrying on trade usually do."

Alpha Hardware & Supply Co. v. Ruby Mines Co., Cal. App. 97, Whiting 1929, p. 515:

> "(7) A debtor is insolvent when he is unable to pay his debts from his own means as they become due. *Southwick v. Moore,* 61 Cal. App. 585 (215 Pac. 704); *First National Bank of Los Angeles v. Maxwell,* 123 Cal. 360 (69 Am. St. Rep. 64, 55 Pac. 980)."

32 *Corpus Juris* 806, states that the word "insolvency" has two meanings:

> "In its general and popular meaning the term denotes the state of one whose entire property and assets, when converted into money without unreasonable haste or sacrifice, are insufficient to pay his debts; * * * But it is frequently used in the more restricted sense to express the inability of a person to pay his debts as they become due in the ordinary course of business."

This petitioner in 1937 was not only unable to pay its debts in the ordinary course of business, but was unable to pay them by hypothecating and pledging all of its assets and income. Congress certainly intended to afford relief to a taxpayer so placed when it said "in receivership and insolvent" and then defined "insolvent" to mean "unable to pay claims of creditors as they mature." With such language in the act, Congress should

not be held to have intended to impose a surtax on a company situated as was this petitioner for *not* doing what, in the first place, *it couldn't do* and what, in the second place, *it sholdn't do,* that is, distribute its income to its own stockholders. I say "couldn't do" because it was entirely under the jurisdiction of the Superior Court and payment of its entire income to its creditors was made on instruction and order of the Court. I say "couldn't do" also because no court in California would permit distribution of profits to stockholders under such circumstances. The California codes, in fact, prohibit and make quasi-criminal declaration of dividends under such circumstances. In addition, the entire income had been assigned to the creditor and belonged to the creditor, as will be shown later in this brief. I say "shouldn't do" from every standpoint, moral, legal, equitable and financial, for reasons that are obvious. The company did the only thing it could and should do—it paid its entire net income to its creditor. After doing so, it still had an indebtedness of $100,250.00, which it had no means within its power at that time to liquidate.

The statute we are here discussing has been repealed. It was too harsh, even in a day of unparalleled harshness in revenue laws. Effect must be given to the words of the statute for the short period in which it still remains effective. But the statute should not be extended beyond its necessary implications. We feel that is what the Board of Tax Appeals has done in this case. Congress never intended to penalize a company in the

position of this petitioner in the year 1937 for not distributing its net income to its own stockholders, and there is ample basis in the language of the act itself to sustain that statement. A number of cases defining insolvency and applying a definition to varying situations have been shown above, but no better definition can be found than the one the Finance Committee itself gave. It is in full accord with the definition long ago given by the Supreme Court of the United States in *Cunningham v. Norton,* 125 U. S. 77, wherein Mr. Justice Bradley said:

> "Secondly: It is objected that the deed of assignment does not, on its face, show that the assignor was insolvent, or in contemplation of insolvency. The obvious answer is that if this is a necessary requirement, the deed does state that the assignor 'is indebted to divers persons in considerable sums of money, which he is at present unable to pay in full.' When a person is unable to pay his debts, he is understood to be insolvent. It is difficult to give a more accurate definition of insolvency. The objection is without foundation."

The Board apparently based its holding against petitioner as to insolvency on three grounds, viz:

1. The receivership was not instituted on the ground of insolvency [Tr. pp. 31 and 33].

2. Book value of assets greatly exceeded liabilities [Tr. p. 33].

3. Petitioner had a net income of $54,101.14 for 1937.

We have already mentioned our reasons for believing the statute does not require the first. If the definition of insolvency given by the Senate Finance Committee be accepted, the second ground is immaterial. The authorities and cases cited so hold, even when *actual* value of assets be considered. But here the Board is considering mere book values, which in this instance are write-up values as of March 1, 1913 [Tr. p. 100]. Values were lower in 1937 than in 1913 [Tr. pp. 100, 101]. No oil depletion had ever been charged against assets on the books [Tr. pp. 94, 95]. The *book* values on which the Board relied are generally discredited by receiver's efforts to raise money without success, and specifically so by the fact that the Security Bank spent considerable time in appraising the assets of the company and then declined to make a loan [Tr. p. 98].

As to the third ground, the statute requires only that at some portion of the taxable year the taxpayer be in receivership and insolvent. Looking at the picture at the beginning of the year, as we are entitled to do, we have a balance owing of $185,000.00 and already an operating deficit of $50,571.97, which deficit would be greatly increased if depletion were charged to surplus, as it should be. Judging by the amounts the receiver, under pressure, had been able to pay to the insurance company during 1935 and 1936, viz., nothing in 1935 and $26,750.00 in 1936, the prospects of petitioner paying its debts then or by March 2, 1937, or at any time in the immediate future, were nil. When to this picture is added the fruitless efforts of the receiver to raise money with which to pay debts, the insolvency of the petitioner, within the meaning intended by Congress, is well established.

II.

The Petitioner's Promissory Note, Combined With the Assignment of Its Lease and the Income Therefrom, Constituted a Contract Restricting Payment of Dividends and Disposing of the Earnings of the Taxable Year Within the Meaning of Section 26 (c) (1) and (2) of the Revenue Act of 1936.

The pertinent portion of Sections 26(c)(1) and 26(c)(2) are set out below:

"SEC. 26. CREDITS OF CORPORATIONS.

"In the case of a corporation the following credits shall be allowed to the extent provided in the various sections imposing tax—

* * * * * * * * *

"(c) * * *

"(1) * * *. An amount equal to the excess of the adjusted net income over the aggregate of the amounts which can be distributed within the taxable year as dividends without violating a provision of a written contract executed by the corporation prior to May 1, 1936, which provision expressly deals with the payment of dividends.

* * * * * * * * *

"(2) * * *. An amount equal to the portion of the earnings and profits of the taxable year which is required (by a provision of a written contract executed by the corporation prior to May 1, 1936, which provision expressly deals with the disposition of earnings and profits of the taxable year) to be paid within the taxable year in discharge of a debt, or to be irrevocably set aside within the taxable year for the discharge of a debt; to the extent that such amount has been so paid or set aside."

In 1929, at the time of giving its note for $175,000.00, petitioner assigned to the insurance company its lease with the Shell Oil Company and the entire income therefrom. It also gave notice to the Shell Oil Company of the assignment. The written assignment was not written into the evidence, but the assignment was proven by secondary evidence without objection [Tr. pp. 86, 101]. It is also contained in the petitioner's written petition for exemption, recited in Board's opinion [Tr. p. 30], and the Board finds as a fact that the assignment was made [Tr. p. 24].

It is basic to this part of the argument to ascertain the effect of such an assignment and the status of earnings after they are so assigned. So far as title is concerned, the answer will be found in the law of California, which is controlling.

Burnett v. Harmel, 287 U. S. 103;

Bankers Pocahantas Coal Co. v. Burnett, 287 U. S. 308.

The lease and income, both present and future, was assignable.

California Civil Code, Sec. 1044:

> *What may be transferred.* Property of any kind may be transferred, except as otherwise provided by this article.

California Civil Code, Sec. 1045:

> *Possibility.* A mere possibility, not coupled with an interest, cannot be transferred.

California Civil Code, Sec. 1458:

> *Rights arising out of obligation transferable.* A right arising out of an obligation is the property of the person to whom it is due, and may be transferred as such.

Silverstein v. Oakland Title Ins. & Guar. Co., 122 Cal. App. 73:

> Future earnings and profits under existing contracts are assignable.

The assignee becomes the owner:

Central Construction Co. v. Hartman, 7 Cal. App. (2d) 103:

> The assignee, to the extent of his interest, is the owner of the thing assigned as security; and there is no merit to the contention that the trust deed, which itself operated as an assignment of said executory contracts of sale, was by way of security, and therefore did not work a transfer of an interest in real property. Citing *Estate of Margaret Phillips, Deceased,* 71 Cal. 285.

Myers v. South Feather Water Co., 10 Cal. 579:

> Where interest in digging contract assigned for security, HELD assignor had no right to demand payment:
>
> "The assignment * * * operating by its present and effectual change of ownership in the subject-matter, the title is supposed in law to remain divested until it be affirmatively shown that the condition of defeasance has happened. It is not unlike

> a chattel mortgage, which conveys the thing mortgaged, with power to collect, hires and to use the chattel until the money secured thereby is paid; and, until payment is proved, all the right of the mortgagor to the mortgaged property passes to the mortgagee."

Change of possession is not essential to validity:

3 *Cal. Jur.*, p. 204:

> Things in action expressly exempted under the code from statutory rule requiring a valid transfer of personal property to be followed by immediate delivery and change of possession, in order to make transfer valid (Civil Code Cal., Sec. 3440). So where an assignment is absolute in its terms and conveys a personal interest in the written evidence of the chose in action, it is complete, and TITLE THERETO IS VESTED in assignee notwithstanding that possession and control of the chose in action are retained by the assignor.

If the assignee becomes the owner of income so assigned, as the above cases and authorities demonstrate, by what theory can the assignee declare a dividend out of such income? It is true for the purpose of normal income tax the income is still technically the income of the assignor and properly taxable to the assignor, because though he should never possess the income, it is being applied for his benefit. But to impose a surtax because the assignor does not declare a dividend out of such assigned income, which is no longer his, is quite a different matter and one that obviously should not be indulged in if any reasonable interpretation of the law permits other treatment.

Discussing Section 26 (c) (1) first, the Board in its Opinion said [Tr. p. 35]:

> "There is nothing to show that the assignment of the Shell Co. oil royalties by petitioner to its creditor, the Pacific Mutual Insurance Co., as further security for the payment of its $175,000 note, in any manner expressly restricted petitioner in the payment of dividends. This assignment is not in evidence and we do not know what written provisions it contained, but the witness who testified in regard to it did not say that the assignment dealt 'expressly with the payment of dividends.' Petitioner does not so contend in its brief. It simply contends that because petitioner had assigned these oil royalties to its creditor, as additional security for the payment of its notes, it was by necessary implication prohibited from the payment of any dividends during the effective period of the assignment."

The Board decided this case soon after the Supreme Court handed down its opinion in *Helvering v. Northwest Steel Rolling Mills, Inc.*, 311 U. S. 46. The Board was doubtless influenced and guided, as it should be, by that decision. But we do not understand the Court's language in that case to go so far as to hold that a specific contract expressly assigning title to income out of which dividends might be declared was not a contract dealing expressly with the declaration of a dividend. In the *Northwest Steel Rolling Mills, Inc.*, case the Supreme Court was dealing with statutorily prohibited dividends and it said:

> "The natural impression conveyed by the words 'written contract executed by the corporation' is that an explicit understanding has been reached, reduced to writing, signed and delivered."

The instant case is not open to that objection because here the parties did make a specific written contract, with a definite understanding, to-wit, a promissory note and assignment of the full ownership in a lease, together with all of the income therefrom. It is true that the Court used further language which appears to lay down a very fine drawn rule on the requirement that a contract shall contain a provision which "expressly deals with the payment of dividends". But the Court did not say that the literal words "payment of dividends" must be used. It said in effect that the *subject* must be expressly dealt with. I should say that a specific contract which transferred the title and ownership of earnings to another is a contract which "expressly deals with the payment of dividends". The right to declare a dividend is a mere incident of ownership. It is one of the sticks in the bundle of rights which go to make up ownership of the earnings. When the bundle is transferred, each stick is transferred. Transfer of title is a transfer of each incident of ownership and expressly so as to each, as much so as if each were conveyed separately.

Passing to Section 26 (c) (2), the contract requirement in that section is as follows:

> "A provision of a written contract executed by the corporation prior to May 1, 1936, which provision expressly deals with the disposition of earnings and profits of the taxable year."

The language used by this petitioner in describing the earnings and profits in the assignment of the lease was "together with all rents due, or to become due" [Tr. p. 30].

The Board of Tax Appeals itself has held that the words "earnings and profits" literally need not be employed to conform to the requirements of the statute.

G. B. R. Oil Company, 40 B. T. A. 738;

Michigan Silica Company, 41 B. T. A. 511.

Treasury Regulations, referring to Section 26 (c) (2), provide:

> "A contractual provision, however, shall not be considered as not expressly dealing with earnings and profits of the taxable year merely because it deals with such earnings and profits in terms of 'net income', 'net earnings', or 'net profits'." Regulations 94, Article 26-2 (c).

We have here then a specific contract in writing, consisting of a promissory note in which the petitioner agrees to pay a certain sum in 1934, and a conveyance to the creditor of title and ownership in the earnings of the taxable year. The contract meets the requirements of the statute in that:

(1) It is a "written contract executed by the Corporation prior to May 1, 1936."

(2) It "expressly deals with the disposition of earnings and profits of the taxable year." By conveying ownership of the earnings to the creditor the Corporation appropriated them to the sole purpose of paying the debt and rendered them unavailable for other purposes. This was a "disposition" and the contract was express.

(3) The amount of earnings sought as a credit was "required . . . to be irrevocably set aside within the taxable year for the discharge of a debt. The assignment of the earnings constituted an irrevocable setting aside and for no purpose other than "for the discharge of a debt."

(4) ". . . to the extent that such amount has been so paid or set aside." The entire royalty earnings were both set aside and paid on the debt within the taxable year.

The note and assignment covered only the oil lease income but this was over 90% of total income. In this regard the statute (Sec. 26 (c) (2)) provides:

> "For the purposes of this paragraph, a requirement to pay or set aside an amount equal to a percentage of earnings and profits shall be considered a requirement to pay or set aside such percentage of earnings and profits."

The fact that the creditor became the actual owner of the earnings by assignment differentiates this case from nearly every decision rendered thus far under Section 26 (c), including those cases decided by the Supreme Court. The *G. B. R. Oil Corporation,* 40 B. T. A. 738, was another case where earnings *were assigned* and the Board in that case upheld the taxpayer. In the *G. B. R.* case the creditor, a bank, did receive the income in the first instance but examination of the case (40 B. T. A. 737 at p. 739) shows that the bank immediately deposited its receipts in the deposit account of the debtor and later

the debtor, after paying expenses, gave the bank a check on the deposit account for an amount to be applied on the debt. In the instant case the creditor permitted the petitioner to collect. The creditor could have required payment to itself direct at any time [Tr. p. 86]. There is no difference in the contracts. The creditor had the same rights under both and actual payment was made under both.

Respectfully submitted,

GEORGE G. WITTER,
Attorney for Appellant.

No. 9824

In the United States Circuit Court of Appeals for the Ninth Circuit

ARTESIAN WATER COMPANY, A CORPORATION, PETITIONER

v.

COMMISSIONER OF INTERNAL REVENUE, RESPONDENT

ON PETITION FOR REVIEW OF THE DECISION OF THE UNITED STATES BOARD OF TAX APPEALS

BRIEF FOR THE RESPONDENT

SAMUEL O. CLARK, Jr.,
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HELEN R. CARLOSS,
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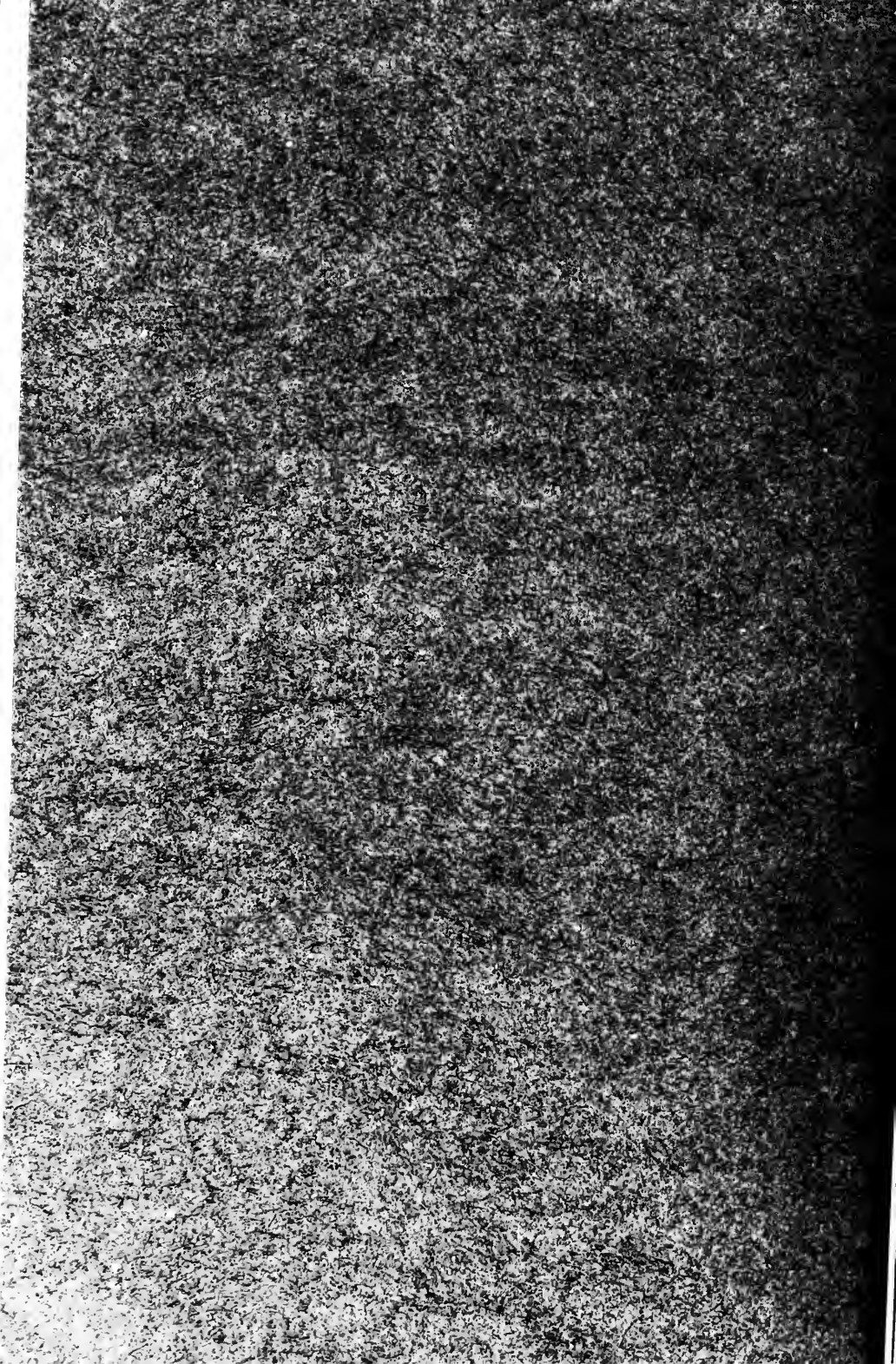

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BRIEF FOR THE RESPONDENT

OPINION BELOW

The opinion of the United States Board of Tax Appeals (R. 21–37) is reported at 43 B. T. A. 408.

JURISDICTION

This case involves deficiencies in income taxes in the calendar year 1937 in the amount of $7,380.33. (R. 38.) The order of the Board was entered January 24, 1941 (R. 37–38), and the taxpayer filed a petition for review on April 16, 1941 (R. 38–41), in accordance with the provisions of Sections 1141 and 1142 of the Internal Revenue Code.

QUESTIONS PRESENTED

The questions presented to this Court are:

1. Whether the taxpayer is entitled to an exemption from the undistributed profits tax by virtue of Section 14 (d) (2) of the Revenue Act of 1936; or

2. If not falling within the exemption, whether the taxpayer is entitled to a credit under either Section 26 (c) (1) or Section 26 (c) (2).

STATUTE AND REGULATIONS INVOLVED

The statute and regulations involved are set forth in the Appendix, *infra,* pp. 14–18.

STATEMENT

On November 12, 1929, the taxpayer, a California corporation (R. 23), refinanced a loan owing to the Pacific Mutual Life Insurance Company, executing a 6 percent promissory note for $175,000 due November 12, 1934. Subsequently another similar note was executed for $35,000. (R. 24, 54–55, 59–60.) Both notes were secured by a mortgage on unimproved farm lands (R. 24, 58), the mortgage providing that it should secure any subsequent loans (R. 68). The original note was further secured by an assignment of a lease of certain oil properties which the Shell Oil Company leased from the taxpayer. However, all royalties from the lease were paid by Shell Oil directly to the taxpayer. A separate agreement was made concerning the $35,000 note to the effect the taxpayer would refrain from declaring any dividends while the note was unpaid. (R. 24–25.) The mortgage covered substantially the major portion of the company's assets, while the lease to

Shell Oil yielded over 90 per cent of the income. (R. 23, 24, 77.)

In July, 1935, the taxpayer was placed in receivership under the California law. The receiver was appointed as a result of a petition filed by a judgment creditor of one of taxpayer's stockholders. The judgment creditor, having acquired stock of the taxpayer at a sheriff's sale, applied to the corporate officers of the taxpayer to transfer the stock to him on the company's books. Upon the refusal of the officers to do so, the judgment creditor petitioned for the appointment of a receiver on the ground that the company's officers were not functioning under California law. The receivership had no connection with taxpayer's ability or disability to pay its debts, nor did the Pacific Mutual have anything to do with it. The taxpayer owed no debts other than current obligations which were paid when due. (R. 25–27.)

Sometime around the middle of the year 1936 a conservator was appointed for the Pacific Mutual and the loans to the taxpayer came under close scrutiny and severe criticism, because of certain interlocking interests between the two companies. (R. 46, 78.)

Nothing was paid on the principal of this obligation until late in 1936. In September of that year an agreement was reached between the receiver and the conservator whereby the time for payment of the loan was extended to March 2, 1937, conditioned upon certain payments being made during the ensuing period. This agreement was evidenced by an exchange of letters. (R. 27, 83.) During 1936 the receiver paid $25,000 on

the notes and made additional payments during 1937, reducing the total balance due to $100,250. The smaller note was paid off in full during 1937 and the larger one in 1938. (R. 61, 55.)

The taxpayer had net income of $54,101 during 1937 on which it paid the normal tax. (R. 33, 113.) This case involves the deficiency asserted by the Commissioner of Internal Revenue in the surtax for the year 1937.

The Commissioner, in his deficiency notice, stated that the taxpayer was not, under the facts presented, entitled to an exemption. A credit of $8,250 representing the amount paid during 1937 on the $35,000 note was allowed as a credit for contracts restricting dividends.[1] The amounts paid on the $175,000 note were not allowed. The Board upheld the Commissioner. (R. 22–23.)

SUMMARY OF ARGUMENT

The Board's finding that the taxpayer was not insolvent is supported by substantial evidence and therefore is conclusive on this Court. Hence, it is not entitled to the exemption from the surtax provided in Section 14 (d) (2). The execution of promissory notes, secured by a mortgage on most of taxpayer's assets and by the assignment of a lease constituting the principal source of taxpayer's income, does not constitute a written contract expressly dealing with the payment of dividends nor a written contract expressly dealing with the disposition of earnings and profits, within the meaning of

[1] There is no reference in this record to the contract upon which this credit was based. However, the amount of the credit granted is not in issue.

Section 26 (c) (1) and 26 (c) (2). Hence the corporation is not entitled to a credit under either of those provisions.

ARGUMENT

I

The taxpayer was not entitled to an exemption under section 14 (d) (2)

Section 14 of the Revenue Act of 1936 imposed a surtax on corporate profits, earned but not distributed during the tax year. Section 14 (d) (2) provided an exemption for corporations in bankruptcy or insolvent and in receivership. Section 26 (c) (1) granted a credit for undistributed profits that could not be distributed during the taxable year as dividends "without violating a provision of a written contract executed by the corporation prior to May 1, 1936, which provision expressly deals with the payment of dividends." Similarly, Section 26 (c) (2) granted a credit for undistributed earnings and profits which were required to be paid or irrevocably set aside within the taxable year for the discharge of a debt by "a provision of a written contract executed by the corporation prior to May 1, 1936, which provision expressly deals with the disposition of earnings and profits for the taxable year."

The first question to be resolved is whether this taxpayer was entitled to an exemption under Section 14 (d) (2). We may concede, for the purposes of this part of the argument, that it is enough if the corporation is insolvent and in receivership and the nature of the receivership proceeding is immaterial. However,

the Commissioner and the Board must determine whether the taxpayer was insolvent. Such a determination is essentially a finding of fact which, if supported by substantial evidence, is conclusive. *Elmhurst Cemetery Co.* v. *Commissioner,* 300 U. S. 37, reversing 83 F. (2d) 4 (C. C. A. 7th); *Oak Woods Cemetery Ass'n.* v. *Commissioner,* 111 F. (2d) 863 (C. C. A. 7th), certiorari denied, 308 U. S. 616. Of course, if there is no evidence to support the Board's finding, this Court would be entitled to reverse. Cf. *United States* v. *Anderson Co.,* 119 F. (2d) 343 (C. C. A. 7th); *Commerce Trust Co.* v. *Woodbury,* 77 F. (2d) 478 (C. C. A. 8th), certiorari denied, 296 U. S. 614; *Central West Public Service Co.* v. *Craig,* 70 F. (2d) 427 (C. C. A. 8th). However, the taxpayer has the burden of presenting substantial evidence to offset the Commissioner's determination. See *Fesler* v. *Commissioner,* 38 F. (2d) 155 (C. C. A. 7th), certiorari denied, 281 U. S. 755; *Brown* v. *Commissioner,* 22 F. (2d) 797 (C. C. A. 5th.)

It cannot seriously be contended that the taxpayer was insolvent in a bankruptcy sense of having liabilities exceeding assets. The balance sheet, as filed with the company's income tax return for the year, showed total assets of $1,162,798, and total liabilities, exclusive of capital stock and surplus, listed at $144,255. Substantially, the same situation had existed at the beginning of the year. (R. 33, 113.) In the taxpayer's brief (p. 16) there is an attempt to discredit the Board's finding on the ground that the figures given above were merely book values as of March, 1913, claiming that the values were less in 1937, and that no depletion for

oil had been charged against assets on the books. The only testimony regarding the value of the assets was that the receiver, admittedly not a real estate man, who "wouldn't know" but "would say" that there would be a substantial difference in such values. (R. 100.) The testimony regarding depletion was to the effect that if the undivided profits at the end of the year of $34,442 had been reduced by the claimed depletion of $44,863, there would be no undivided profits balance but a deficit of approximately $10,400. Admitting the mathematical accuracy of this calculation, it is submitted that it has no effect on the present issue. A deduction from undivided profits would not affect the balance between assets and liabilities, exclusive of capital stock and surplus. Clearly, there is no evidence here which the Board would have been justified in using to offset the balance sheet figures. Nor is there any evidence in the record to warrant a finding that the assets were overvalued on the company's books by something over a million dollars which would be the adjustment necessary to make liabilities exceed assets.

Therefore, the principal question under the exemption section is whether the taxpayer was insolvent in the so-called equity sense—that is, was it unable to meet its currently maturing obligations. The problem was well posed in *United States* v. *Anderson Co., supra,* where the court said (p. 345):

> The practical question is—Under what circumstances may a court say that a corporation is unable to pay its debts as they fall due in the usual course of trade or business?

It will be noted that in defining insolvency the authorities stress the fact that it means inability to pay debts as they become due in the ordinary course of business. See *Dutcher* v. *Wright,* 94 U. S. 553; and *Cincinnati Equipment Co.* v. *Degnan,* 184 Fed. 834 (C. C. A. 6th). The record in this case shows that all debts of this company were paid except the obligation owed to the Pacific Mutual (R. 97), which debt originally fell due in November, 1934. The record is somewhat indefinite with regard to what steps, if any, were taken to secure an extension or to refinance the debt from the due date until 1936. It may be that originally a request for an extension was refused (R. 84) but insofar as there is any substantial evidence in this record it is evident that the negotiations were not seriously undertaken until 1936, although the receiver had been appointed in July, 1935. (R. 77.) At no time did the taxpayer become involved in any legal proceedings because of its inability to pay its bills. (R. 97.) Nothing was paid on the principal of this obligation from the time the loan was made until late in the year 1936. (R. 85.) It was around the middle of 1936 that a conservator had been appointed for the insurance company (R. 46, 78) and it would appear that it was only after that time that the creditor began to be really concerned about the liquidation of the loan (R. 78). There is certainly substantial evidence to support a finding that this obligation was not "currently maturing." Since the debt had originally become due in 1934 and the creditor took no steps for its collection other than to grant an extension in September, 1936, until March, 1937, it is quite

apparent that the creditor was acquiescent in the installment payment of this debt. Moreover, after March, 1937, the creditor continued to permit the debtor to pay off the debt in installments. From these facts it would be impossible to consider that this obligation was one falling due in the ordinary course of business. In effect and in reality, the creditor was placing reliance upon the debtor's ultimate ability to pay and was not demanding immediate payment. This clearly amounts to an extension of credit. When able to meet its obligations by reasonable use of credit a debtor is not insolvent. *United States* v. *Anderson Co., supra; Coffman* v. *Publishing Co.,* 167 Md. 275, 173 Atl. 248; *Long* v. *Republic Varnish Enamel &c., Co.,* 115 N. J. Eq. 212, 169 Atl. 860. Since the taxpayer was neither insolvent, in the sense of an excess of liabiilties over assets, nor insolvent, in the sense that it could not meet its current obligations, it was not within the terms of the exemption.

As an alternative and additional argument, it is submitted that the taxpayer did not come within the exemption since the receivership intended by this section was obviously intended to mean one caused by financial difficulties and not one arising from disputes between the stockholders, charges of mismanagement, failure to obey the laws, etc. As shown by the Committee Reports on this bill, the intent of Congress was to exempt those corporations in a weak financial condition.[2] In

[2] Adequate safeguards are provided in the bill to prevent unreasonable taxation of incomes in the case of corporations in distress or with inadequate earnings to take care of their immediate needs. * * * H. Rep. No. 2475, 74th Cong., 2d Sess.,

the instant case the receivership had no connection with the financial condition of the taxpayer; it arose out of a suit against a stockholder by his judgment creditor and the subsequent officers of the company. (R. 25.) In order for a company to use this exemption, it must be in receivership as well as insolvent. *Cooperative Pub. Co.* v. *Commissioner,* 115 F. (2d) 1017 (C. C. A. 9th).

II

The taxpayer was not entitled to either of the credits granted in Section 26 (c) (1) or 26 (c) (2)

The theory of the taxpayer's case is that by giving the mortgage note for $175,000 and assigning the lease to the creditor it became entitled to the credit allowed under Section 26 (c) (1) or (2). It is well settled that a credit provision in the tax law should be as strictly construed as an exempting provision. *Helvering* v. *Northwest Steel Mills,* 311 U. S. 46; *Helvering* v. *Inter-Mountain Insurance Co.,* 294 U. S. 686; *Crane-Johnson Co.* v. *Commissioner,* 105 F. (2d) 740 (C. C. A. 8th), affirmed, 311 U. S. 54. The *Northwest Steel Mills* case is directly contrary to the taxpayer's contention that Section 26 (c) is to be liberally construed. There the Court stated (p. 49):

> * * * Congress indicated that any exempted prohibition against dividend payments must be expressly written in the executed contract. * * * the granted credit can only

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p. 4 (1939–1 Cum. Bull. (Part 2) 667, 669). To the same effect is S. Rep. No. 2156, 74th Cong., 2d Sess., p. 14 (1939–1 Cum. Bull. (Part 2), 678).

result from a provision which "expressly deals with the payment of dividends."

There was nothing in the mortgage, nor insofar as the record reveals in the assignment, that "expressly deals with the payment of dividends." Hence, Section 26 (c) (1) clearly does not apply.

It matters not what was the effect of the state law concerning the mortgage and assignment, since it is well settled that statutes specifically prohibiting dividend payments do not constitute written contract executed by the corporation prohibiting such payments within the meaning of Section 26 (c) (1). *Helvering* v. *Northwest Steel Mills, supra; Utah Hotel Co.* v. *Hinckley,* 115 F. (2d) 920 (C. C. A. 10th); *Bastian Bros. Co.* v. *McGowan,* 113 F. (2d) 489 (C. C. A. 2d), certiorari denied, 311 U. S. 702; and *Cooperative Pub. Co.* v. *Commissioner, supra.* The whole theory of these authorities is that although the corporation might not be able to declare dividends because of the effect of some superior force upon it, the credit was not allowable except when there was a written contract executed by the corporation dealing expressly and not impliedly with the question.

Similar principles apply in determining whether a credit is allowable under Section 26 (c) (2). In order to be entitled to a credit under that section the corporation must have executed prior to May 1, 1936, a written contract containing a specific provision requiring a portion of its earnings and profits of the taxable year to be paid or set aside in discharge of a debt. There is no such contract here.

Any promise to make periodic payments on an indebtedness would naturally be restrictive as to the earnings and profits of the debtor but it can hardly be contended that Congress meant to include within this section all promises to liquidate just debts. It was intended that the exemption apply only when an explicit contract required it to apply specifically a portion of its earnings for the current year to the payment of a debt. Here the royalties from the lease were paid directly to the taxpayer and the taxpayer concedes that it was properly required to report the royalties as its income. (Br. 20.) Although the creditor might, by virtue of the state law, be entitled to demand them from the taxpayer, it is the force of the state law which gives him this right and not an express contract dealing with the disposition of the earnings and profits. See *Helvering* v. *Northwest Steel Mills, supra.* The income from the lease was assigned as security for the loan. (R. 24.) If the taxpayer chose to pay the creditor from other sources he would not care from what source he were paid. Clearly this assignment as security was not an express contract requiring the debtor to pay or irrevocably set aside a portion of the earnings during the taxable year.

If the taxpayer's theory were applied literally, it would follow that all payments on account of legally owing debts would constitute a credit against this tax, since any payment on a debt will have a restrictive effect on the company's profits. It is a rare corporation that is not making payments on borrowed capital. But Congress has not provided relief in such cases. It

has stated with meticulous care the circumstances under which a credit would be allowed. The allowance of credits and deductions is within the discretion of Congress and the language of the statute cannot be stretched to cover this case because of any alleged hardship on the taxpayer. See *Helvering* v. *Northwest Steel Mills, supra.*

Moreover, the hardship here is more imaginary than real. This corporation was a profitable going concern during the year in question and should not escape this tax merely because during those years it repaid a large amount of its indebtedness. If there could be any unfairness in the instant case, it would be the unfairness to other corporations which paid this tax while making a profit although not in a sound enough financial condition to repay their capital investments.

CONCLUSION

The decision of the Board that the taxpayer was not exempt and was not entitled to a credit for the amounts paid was correct and should be affirmed.

Respectfully submitted.

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SHERLEY EWING,
Special Assistants to the Attorney General.

AUGUST, 1941.

APPENDIX

Revenue Act of 1936, c. 690, 49 Stat. 1648:

SEC. 14. SURTAX ON UNDISTRIBUTED PROFITS.

* * * * *

(b) *Imposition of Tax.*—There shall be levied, collected, and paid for each taxable year upon the net income of every corporation a surtax equal to the sum of the following, subject to the application of the specific credit as provided in subsection (c):

7 per centum of the portion of the undistributed net income which is not in excess of 10 per centum of the adjusted net income.

* * * * *

(d) *Exemption From Surtax.*—The following corporations shall not be subject to the surtax imposed by this section:

* * * * *

(2) Domestic corporations which for any portion of the taxable year are in bankruptcy under the laws of the United States, or are insolvent and in receivership in any court of the United States or of any State, Territory, or the District of Columbia.

* * * * *

SEC. 26. CREDITS OF CORPORATIONS.

In the case of a corporation the following credits shall be allowed to the extent provided in the various sections imposing tax—

* * * * *

(c) *Contracts Restricting Payment of Dividends.*—

(1) PROHIBITION ON PAYMENT OF DIVIDENDS.—An amount equal to the excess of the adjusted net income over the aggregate of the amounts

which can be distributed within the taxable year as dividends without violating a provision of a written contract executed by the corporation prior to May 1, 1936, which provision expressly deals with the payment of dividends. If a corporation would be entitled to a credit under this paragraph because of a contract provision and also to one or more credits because of other contract provisions, only the largest of such credits shall be allowed, and for such purpose if two or more credits are equal in amount only one shall be taken into account.

(2) DISPOSITION OF PROFITS OF TAXABLE YEAR.—An amount equal to the portion of the earnings and profits of the taxable year which is required (by a provision of a written contract executed by the corporation prior to May 1, 1936, which provision expressly deals with the disposition of earnings and profits of the taxable year) to be paid within the taxable year in discharge of a debt, or to be irrevocably set aside within the taxable year for the discharge of a debt; to the extent that such amount has been so paid or set aside. For the purposes of this paragraph, a requirement to pay or set aside an amount equal to a percentage of earnings and profits shall be considered a requirement to pay or set aside such percentage of earnings and profits. As used in this paragraph, the word "debt" does not include a debt incurred after April 30, 1936.

* * * * *

Treasury Regulations 94, promulgated under the Revenue Act of 1936:

ART. 14–1. *Surtax on undistributed profits of corporations.*—

* * * * *

A domestic corporation is not subject to the surtax on undistributed profits if for any portion of its taxable year—

(1) it is in bankruptcy under the laws of the United States; or

(2) it is insolvent and in receivership in any court of the United States or any State, Territory, or the District of Columbia.

* * * * *

ART. 26–2. *Credit in connection with contracts restricting payment of dividends.*—(a) The credit provided in section 26 (c) with respect to contracts restricting the payment of dividends is not available under every contract which might operate to restrict the payment of dividends, but only with respect to those provisions of written contracts executed by the corporation prior to May 1, 1936, which satisfy the conditions prescribed in the Act. The charter of a corporation does not constitute a written contract executed by the corporation within the meaning of section 26 (c). The provisions recognized by the Act are of two general types, as folows:

(1) Those which come within section 26 (c) (1), in that they prohibit or limit the payment of dividends during the taxable year; and

(2) Those which come within section 26 (c) (2), in that they require the payment, or irrevocable setting aside, within the taxable year, of a specified portion of the earnings or profits of the taxable year for the discharge of a debt incurred on or before April 30, 1936.

* * * * *

(b) *Prohibition on payment of dividends.*—The credit provided in section 26 (c) (1) is allowable only with respect to a written contract executed by the corporation prior to May 1, 1936, which expressly deals with the payment of dividends and operates as a legal restriction upon the corporation as to the amounts which it can distribute within the taxable year as dividends. If an amount can be distributed within the taxable year as a dividend—

(1) in one form (as, for example, in stock or bonds of the corporation) without violating the

provisions of a contract, but can not be distributed within the taxable year as a dividend in another form (as, for example, in cash) without violating such provisions, or

(2) at one time (as, for example, during the last half of the taxable year) without violating the provisions of a contract, but can not be distributed as a dividend at another time within the taxable year (as, for example, during the first half of the taxable year) without violating such provision—

then the amount is one which, under section 26 (c) (1), can be distributed within the taxable year as a dividend without violating such provisions.

The credit provided in section 26 (c) (1) is equal to the excess of the adjusted net income, as defined in section 14 (a), over the aggregate of the amounts which can be distributed within the taxable year without violating the provisions of such contract. The requirement that the provisions of the contract expressly deal with the payment of dividends is not met in case (1) a corporation is merely required to set aside periodically a sum to retire its bonds, or (2) the contract merely provides that while its bonds are outstanding the current assets shall not be reduced below a specified amount.

* * * * *

(c) *Disposition of profits of taxable year.*— Under the provisions of section 26 (c) (2), a corporation is allowed a credit in an amount equal to that portion of the earnings and profits of the taxable year which, by the terms of a written contract executed by the corporation prior to May 1, 1936, and expressly dealing with the disposition of the earnings and profits of the taxable year, it is required within the taxable year to pay in, or irrevocably to set aside for, the discharge of a debt incurred on or before April 30, 1936. The credit is limited to that amount

which is actually so paid or irrevocably set aside during the taxable year pursuant to the requirements of such a contract.

Only a contractual provision which expressly deals with the disposition of the earnings and profits of the taxable year shall be recognized as a basis for the credit provided in section 26 (c) (2). A corporation having outstanding bonds is not entitled to a credit under a provision merely requiring it, for example, (1) to retire annually a certain percentage or amount of such bonds, (2) to maintain a sinking fund sufficient to retire all or a certain percentage of such bonds by maturity, (3) to pay into a sinking fund for the retirement of such bonds a specified amount per thousand feet of timber cut or per ton of coal mined, or (4) to pay into a sinking fund for the retirement of such bonds an amount equal to a certain percentage of gross sales or gross income. Such provisions do not expressly deal with the disposition of earnings and profits of the taxable year. A contractual provision, however, shall not be considered as not expressly dealing with the disposition of earnings and profits of the taxable year merely because it deals with such earnings and profits in terms of "net income," "net earnings," or "net profits."

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No. 9826

United States

Circuit Court of Appeals

For the Ninth Circuit.

GIN SOON GING,

Appellant,

vs.

WILLIAM A. CARMICHAEL, District Director of Immigration and Naturalization Service,

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Transcript of Record

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*Page numbering appearing at foot of page of original certified Transcript of Record.

In the United States District Court in and for the Southern District of California
Central Division

No. 14531 M

In the Matter of the Application of
GIN SOON GING
For a Writ of Habeas Corpus

PETITION FOR WRIT OF HABEAS CORPUS

To the Honorable Judge in the above-entitled Court, Your Petitioner, Gin Ting, Respectfully States:

I.

That he was born in the United States and that under the Constitution thereof, he is a citizen of the United States; that as evidence of his said American citizenship, he holds United States Citizen's Certificate of Identity No. 5888 issued to him by the Commissioner of Immigration and Naturalization at San Francisco, California, on November 7, 1911; and that he has never expatriated himself as such a citizen;

II.

That he has a son by the name of Gin Soon Ging born to him and his wife in China on May 25, 1926, and that under the provisions of Section 1993 of the Revised Statutes, the said Gin Soon Ging is also a citizen of the United States; and that on or about June 30, 1940, his said son came to the port

of San Pedro, California and applied to the Immigration and Naturalization Authorities thereof for admission so as to join the petitioner in this country;

III.

That on July 9, 1940, a board of special inquiry was convened to hear the application of the aforesaid Gin Soon Ging for admission to the United States as a natural born citizen thereof; that your petitioner and his clansman Gin Wing Fun appeared [2] before the said board as witnesses in the applicant's behalf; that after hearing the testimony concerning the applicant's ancestors, parents, brothers, and other relatives, his family home, ancestral village and schooling in China, and many other collateral matters pertaining to the applicant's claimed relationship to your petitioner, the board of special inquiry denied the said application, not because of any inconsistencies in the testimony between your petitioner and the said Gin Soon Ging but because of certain discrepancies between your petitioner and his older son Gin Hong Goon in certain proceedings which took place in 1931 and 1937 to which the present applicant Gin Soon Ging was not a party;

IV.

That the board of special inquiry upon receipt of an anonymous letter to the effect that the applicant was your petitioner's grandson instead of his son, reopened the hearing on July 23, 1940 in

order to question the parties hereto along the line of the information so anonymously received; and that at the conclusion of this supplementary hearing, the applicant was again excluded;

V.

That an appeal from the excluding decision by the board of special inquiry was forthwith taken to the Board of Review of the Attorney-General, but the appellate board on September 24th, 1940 dismissed the appeal and instructed the District Director of Immigration and Naturalization for the port of San Pedro, California to deport the said Gin Soon Ging on the first available steamer leaving for China; that unless this Honorable Court intervene, Gin Soon Ging will be promptly taken out of the United States; and that the aforesaid proceedings involved a question of citizenship and denial of a fair hearing to an American citizen, over which this Honorable Court has undisputed jurisdiction,—Wong Hai Sing vs. Nagle, C. C. A. 9, 49 Fed. (2d) 1016; and,

VI.

That the evidence adduced before the Immigration Authorities [3] established to a reasonable certainty that the applicant Gin Soon Ging is the son of your petitioner in that there was not a single discrepancy in the testimony concerning the applicant's family history, relatives, home life, ancestral

village, and schooling, the movements of various members of applicant's father's family, important events as well as collateral matters which were commonly known to members of this family; that it was arbitrary and unfair for the Immigration Authorities to exclude the applicant where the evidence submitted has so conclusively established the relationship of father and son between your petitioner and the said Gin Soon Ging—Jue Yim Ton vs. Nagle, C. C. A. 9, 48 Fed. (2d) 752; that the immigration tribunals may ascertain facts in any reasonable and fair way they see fit, but they cannot reject sworn, consistent, unimpeached and uncontradicted testimony without real reason which fair-minded persons would regard as adequate—Ward vs. Flynn ex rel Yee Gim Lung, 74 Fed. (2d) 145; that the discrepancies developed in the hearings of Gin Hong Goon in 1931 and 1937 to which the present applicant Gin Soon Ging was not a party, utilized by the Immigration Authorities to exclude the applicant conclusively showed unfairness and prejudice—Flynn ex rel Chin King vs. Tillinghast, 32 Fed. (2d) 359; Ex parte Ng Bin Fon, 20 Fed. (2d) 1014; and U. S. ex rel Fong Lung Sing vs. Day, 29 Fed. (2d) 619; and, that it was unfair and a violation of the due process of law for the Immigration Authorities to base an excluding decision on mere suspicion brought about by an anonymous letter—Wong Gook Chun vs. Proctor, C. C. A. 9, 84 Fed. (2d) 763.

VII.

Your petitioner further states that the said Gin Soon Ging has been since July 9th, 1940 and is now being held in detention at the Immigration Station at San Pedro, California in the custody of [4] William A. Carmichael, District Director of Immigration and Naturalization, for which reason, the said Gin Soon Ging is unable to verify this petition, so your petitioner as his father therefore verifies this petition in his behalf.

Wherefore your petitioner prays that a writ of habeas corpus be issued and directed to the aforesaid District Director of Immigration and Naturalization as respondent herein, commanding him to hold the body of the said Gin Soon Ging within the jurisdiction of this Honorable Court and to present the said body before this Court at a time and place to be specified in the said order, together with the time and cause of his detention, so that the same may be inquired into to the end that the said Gin Soon Ging may be restored to his liberty and go hence without day.

Dated at Los Angeles, California, this 25th day of September, 1940.

Y. C. HONG,

Attorney for Petitioner.

State of California,
County of Los Angeles—ss.

Gin Ting, being duly sworn, deposes and states: That he is the petitioner named in the foregoing petition; that the same has been read and explained to him and that he knows the contents thereof which is true of his own knowledge except those matters which are therein stated on information and belief, and as to such matters, he believes the same to be true.

GIN TING,

Petitioner.

Subscribed and Sworn to before me this 25th day of September, 1940.

[Seal] Y. C. HONG,

Notary Public.
Los Angeles, California
September ....., 1940. [5]

Let the writ issue as prayed for returnable before United States District Judge Paul J. McCormick on the 7th day of October 1940 at 2 o'clock in the afternoon.

PAUL J. McCORMICK,
United States District Judge.

Dated Sept. 25, 1940 at 2:10 P. M.

[Endorsed]: Filed Sep. 25, 1940. R. S. Zimmerman, Clerk. By P. D. Hooser, Deputy. [6]

United States District Court
Central Division, Southern District of California

[Title of Cause.]

HABEAS CORPUS

The President of the United States of America
To William A. Carmichael, District Director of Immigration and Naturalization, Los Angeles, California—Greeting:

You Are Hereby Commanded, that the body of Gin Soon Ging, by you restrained of his liberty, as it is said detained by whatsoever names the said Gin Soon Ging may be detained, together with the day and cause of being taken and detained, you have before the Honorable Paul J. McCormick, Judge of the United States District Court in and for the Southern District of California, at the court room of said Court, in the City of Los Angeles at 2:00 o'clock p. m., on the 7th day of October, 1940, then and there to do, submit to and receive whatsoever the said Judge shall then and there consider in that behalf; and have you then and there this writ.

Witness the Honorable Paul J. McCormick, United States District Judge at Los Angeles, California, this 25th day of September, A. D. 1940,

[Seal] R. S. ZIMMERMAN,
Clerk.

By GEO. E. RUPERICH,
Deputy Clerk.

[Endorsed]: Filed Oct. 7, 1940. R. S. Zimmerman, Clerk. By B. B. Hansen, Deputy Clerk. [7]

[Title of District Court and Cause.]

RETURN TO WRIT OF HABEAS CORPUS

I, William A. Carmichael, District Director of U. S. Immigration and Naturalization Service, Los Angeles, California District No. 20, Respondent herein, for my Return to Writ of Habeas Corpus issued herein and in compliance with the said Writ of Habeas Corpus, now produce the body of Gin Soon Ging on this 7th day of October, 1940 before this Honorable Court, and for my Return to said Writ deny that I am unlawfully imprisoning and detaining and confining and restraining the liberty of the aforesaid Gin Soon Ging.

For further Return to said Writ, Respondent admits that the said Gin Soon Ging arrived from China at the Port of San Pedro, California the 30th day of June, 1940 on the SS "President Cleveland" and made application for admission into the United States, and certifies that the true cause of said Gin Soon Ging's detention is the finding and order of a duly and regularly constituted Board of Special Inquiry denying him admission into the United States made July 9, 1940, and the order of the Department of Justice, Washington, D. C., made on or about September 24, 1940 confirming the decision of the said Board of Special Inquiry and ordering the return of said Gin Soon Ging to the country whence he came; that Respondent was preparing to return the said Gin Soon Ging to

the country whence he came when this Writ of Habeas Corpus was issued.

For further Return, Respondent makes a part hereof Department of Justice File No. 56040/574, duly certified, containing transcript of the testimony and summary and findings of the Board of Special Inquiry, San Pedro, California and summary and findings of the Board of Immigration Appeals, Washington, D. C.; also certain [8] U. S. Immigration and Naturalization Service records, identified by file numbers: 10508/10558, 25882/4-4, 30348/4-13, 37221/7-27 (San Francisco, California); 7032/2754 (Seattle, Washington); 31160/503 (San Diego, California); 1521/506, 1521/310, 1522/18 (Tucson, Arizona); Exhibits "A" and "B", and a group photograph.

Respectfully submitted,

WILLIAM A. CARMICHAEL,

District Director of U. S. Immigration and Naturalization Service, Los Angeles, California, District No. 20, Respondent.

[Endorsed]: Filed Oct. 7, 1940. R. S. Zimmerman, Clerk. By B. B. Hansen, Deputy Clerk. [9]

[Title of District Court and Cause.]

TRAVERSE TO RETURN

To the Honorable United States District Judge, now presiding in the United States District Court, in and for the Southern District of California, Central Division,

Your Petitioner by way of traverse to the Respondent's Return herein respectfully alleges:

I

That he realleges and incorporates herein each and every allegation contained in his Petition verified the 25th day of September, 1940; and

II

That the denial contained in the said Return is only a conclusion of law and does not show facts sufficient to warrant the restraint, detention, and contemplated deportation of the said Gin Soon Ging by the Respondent;

Wherefore, it is respectfully submitted that the Writ should be sustained and Gin Soon Ging be discharged from the custody of the Respondent.

Dated at Los Angeles, California, this 10th day of October, 1940.

Y. C. HONG
Attorney for Petitioner. [10]

United States of America
State of California
County of Los Angeles—ss.

Gin Ting, Being Duly Sworn, Deposes and States that he is the petitioner in the foregoing traverse; that same has been read and explained to him and that he knows the contents thereof; that the same is true of his own knowledge except as to those matters which are therein stated on his information and belief, and as to those matters, he believes it to be true.

GIN TING
Petitioner.

Subscribed and Sworn to Before Me This 10th day of October, 1940.

[Seal] Y. C. HONG
Notary Public, Los Angeles County

[Endorsed]: Filed Oct. 10, 1940. [11]

At a stated term, to wit: The February Term, A. D. 1941 of the District Court of the United States of America, within and for the Central Division of the Southern District of California, held at the Court Room thereof, in the City of Los Angeles on Wednesday the 2nd day of April in the year of our Lord one thousand nine hundred and forty-one.

Present:

The Honorable: Campbell E. Beaumont, District Judge.

No. 14531-B Crim.

In the Matter of the Petition of
GIN SOON GING

for a Writ of Habeas Corpus

This matter having heretofore come before the Court and documentary evidence having been submitted and counsel having submitted written briefs and the Court having fully considered the same and being fully advised as to the facts and the law, now denies petition for Writ of Habeas Corpus and dismisses said Writ. [13]

United States District Court
Southern District of California
Central Division

No. 14531-B

In the Matter of
GIN SOON GING

MEMORANDUM AND ORDER

The writ challenges a denial of admission to the United States of Gin Soon Ging, a Chinese boy, who claims to be a son of a native United States citizen. The Board of Special Inquiry held that

the relationship had not been established, and upon appeal its decision was affirmed by the Board of Review.

After a study of the record herein the Court cannot say that the Board of Special Inquiry committed a manifest abuse of the power and discretion conferred upon it. In this case the evidence is such that reasonable men might differ as to its probative effect. It was the Board's duty to determine such effect, and it cannot be said that its decision, which represented the unanimous agreement of its members, was reached unfairly or arbitrarily. In such circumstances its decision will not be disturbed. Lum Sha You v. United States (C. C. A. 9th), 82 Fed. (2d) 83; Quon Quon Poy v. Johnson, 273 U. S. 352; United States v. Ju Toy, 198 U. S. 253; Chin Yow v. United States, 208 U. S. 8; Chin Share Nging v. Nagle, 27 Fed. (2d) 848; Mui Sam Hun v. United States, 78 Fed. (2d) 612.

Petition is denied and the writ discharged. April 1, 1941.

BEAUMONT, J.

[Endorsed]: Filed Apr. 10, 1941. [14]

[Title of District Court and Cause.]

NOTICE OF APPEAL

To the Clerk of the above-entitled Court, to William A. Carmichael, District Director of Immigration and Naturalization, and to William Fleet Palmer, Esq., United States Attorney, Attorney for Respondent:

You and each of you will please take notice that Gin Soon Ging, the applicant in the above-entitled matter, hereby appeals to the United States Circuit (*Court*) of Appeals for the Ninth Circuit, from the Order and Judgment rendered, made and entered herein on April 2, 1941, discharging the writ of habeas corpus.

April 11th, 1941, Los Angeles, California.

Y. C. HONG
Attorney for Petitioner

Received Copy of the Within Notice of Appeal this 11th day of April, 1941.

RUSSELL LAMBEAU,
By MMH

Received Copy of the Within Notice of Appeal this day of April, 1941.

A. DI GIROLAMO,
Asst. U. S. Atty.

Copy mailed to District Director 4/11/41, E. L. S.

[Endorsed]: Filed Apr. 11, 1941. [15]

[Title of District Court and Cause.]

STATEMENT OF POINTS ON WHICH APPELLANT INTENDS TO RELY AND DESIGNATION OF THE PARTS OF RECORD WHICH APPELLANT THINKS NECESSARY FOR THE CONSIDERATION THEREOF.

Comes now Gin Soon Ging, the Appellant in the above-entitled matter, respectfully stating that he intends to rely upon the following points on which the District Court erred, to-wit:

I

In holding that the Board of Special Inquiry at the port of San Pedro, California, did not commit a manifest abuse of the power and discretion conferred upon it, whereas the minutes of the administrative proceedings showed that the said Board's finding to the effect that the appellant was Gin Ting's inadmissible grandson was only based upon anonymous information instead of substantial evidence;

II

In holding that the hearing accorded by the Board of Special Inquiry at San Pedro, California, was not unfair and arbitrary whereas the record of the administrative proceedings showed that the said Board's dissatisfaction as to the appellant's claim of relationship to his alleged father, Gin Ting, was based solely upon certain discrepancies between his alleged father and alleged brother Gin Hong Goon developed in certain immigration proceedings had in 1931 and 1937 to which the present appellant was

not a party and on a matter which did not concern the appellant or his relationship to his alleged father Gin Ting;

III

In failing to hold that the consistent and unimpeached testimony of the appellant and his alleged father, Gin Ting, and other uncontradicted [16] evidence of record submitted to the Board of Special Inquiry at San Pedro, California, had reasonably established his claimed relationship to his alleged father Gin Ting; and,

IV

In dismissing the writ of habeas corpus after it was affirmatively shown that the Immigration Authorities had manifestly abused its power and discretion, and arbitrarily and unfairly denied to the appellant admission to his own country.

V

Therefore, the appellant deems it necessary to, and does hereby request that all the original immigration files and records heretofore submitted as exhibits before the District Court be made exhibits before the Circuit Court of Appeals for the Ninth Circuit by filing the same with the Clerk of the said appellate court in accordance with the stipulations adopted on April 25, 1941, by and between the parties hereto.

Dated this 25th day of April, 1941, at Los Angeles, California.

Y. C. HONG
Attorney for Appellant

[Endorsed]: Filed Apr. 25, 1941. R. S. Zimmerman, Clerk. By P. D. Hooser, Deputy. [17]

[Title of District Court and Cause.]

STIPULATION AND ORDER REGARDING ORIGINAL RECORDS AND FILES OF THE DEPARTMENT OF JUSTICE.

It is hereby stipulated and agreed by and between Y. C. Hong, Attorney for Appellant herein, and William Fleet Palmer, Attorney for the Appellee herein, that the original files and records of the Department of Justice covering the application of the above-named party, which were files in the hearings in the above-entitled cause, may be by the Clerk of this court sent to the Clerk of the Circuit Court of Appeals for the Ninth Circuit, as part of the appellate record, in order that the said original immigration files may be considered by the Circuit Court of Appeals for the Ninth Circuit in lieu of a certified copy of the said records and files, and that the same need not be printed.

Dated this 25th day of April, 1941, at Los Angeles, California.

Y. C. HONG
Attorney for Appellant
WM. FLEET PALMER
United States Attorney
By ATTILIO DI GIROLAMO
Asst. United States Attorney
Attorneys for Appellees

On this 25th day of Apr., 1941.
It is so ordered.

PAUL J. McCORMICK
United States District Judge [18]

[Title of District Court and Cause.]

STIPULATION AND ORDER IN RE PRINTING OF TRANSCRIPT OF RECORD

It is hereby stipulated and agreed by and between the parties to the above-entitled cause, through their respective counsel, that the Clerk of the above-entitled Court, in preparing the printed transcript of record on appeal, may omit the heading of all papers filed except the citation, petition for writ of habeas corpus, and assignments of error, substituting in the place and stead thereof the phrase "Title of Court and Cause", and that the said Clerk may omit all backs of documents except the filing endorsements.

Dated this 25th day of April, 1941, at Los Angeles, California.

Y. C. HONG
Attorney for Appellant
WM. FLEET PALMER
United States Attorney
By ATTILIO DI GIROLAMO
Asst. United States Attorney
Attorneys for Appellee

It is so ordered.

Apr. 25th, 1941.

PAUL J. McCORMICK
United States District Judge

[Endorsed]: Filed Apr. 25, 1941. R. S. Zimmerman, Clerk. By P. D. Hooser, Deputy. [19]

[Title of District Court and Cause.]

DESIGNATION OF RECORD ON APPEAL

To the Clerk of the Said Court:

Please prepare and duly authenticate the transcript of the following portions of the record in the above-entitled case for appeal to the United States Circuit Court of Appeals for the Ninth Circuit;

1. Petition for Writ of Habeas Corpus and Order granting writ;
2. Writ of Habeas Corpus;
3. Return to writ of Habeas Corpus;
4. Traverse to Return;

5. Minute and Memorandum and Order of District Court discharging writ;

6. Notice of Appeal;

7. Cost Bond on Appeal;

8. Stipulation and Order Regarding Original Records and Files of the Department of Justice;

9. Stipulation and Order in re Printing of Transcript of Record;

10. Statement of Points on Which Appellant Intends to Rely and Designation of the Parts of Record Which Appellant Thinks Necessary for the Consideration Thereof.

11. Designation of Record on Appeal.

April 25, 1941.

Y. C. HONG
Attorney for Petitioner and Appellant.

Approved:

WM. A. CARMICHAEL H
District Director of Immigration
Respondent-Appellee.

WM. FLEET PALMER
United States Attorney
By ATTILIO DI GIROLAMO
Asst. United States Attorney

[Endorsed]: Filed Apr. 25, 1941. R. S. Zimmerman, Clerk, by P. D. Hooser, Deputy. [21]

[Title of District Court and Cause.]

COST BOND ON APPEAL

Know All Men by These Presents:

That the undersigned Fidelity and Deposit Company of Maryland is held and firmly bound unto the United States of America, in the full and just sum of Two Hundred and Fifty Dollars ($250.00), to be paid to the United States of America, or their attorney, successors or assigns, to which payment, well and truly to be made, the undersigned binds himself, his heirs, executors and administrators, jointly and severally by these presents.

Sealed with his seal and dated this 25th day of April, 1941, at Los Angeles, California.

Whereas, lately in a habeas corpus proceeding in the United States District Court for the Southern District of California, Central Division, between the petitioner Gin Soon Ging and the respondent William A. Carmichael, District Director of Immigration and Naturalization with supervision over the port of San Pedro, California, as aforesaid, an order, judgment and decree was rendered by the said Court on the 1st day of April, 1941, against the said Gin Soon Ging, discharging the writ of habeas corpus and remanding the said petitioner to the custody of the respondent for deportation, and the said petitioner Gin Soon Ging thereupon on the 11th day of April, 1941, filed his notice of appeal with the Clerk of the said Court to have the United

States Circuit Court of Appeals for the Ninth Circuit, to review and reverse the said order, judgment and decree in the aforesaid habeas corpus proceeding.

Now, the condition of the above obligation is such that if the said Gin Soon Ging shall prosecute his appeal to effect and answer all costs if [23] he fails to make his plea good, then the above obligation to be void, else to remain in full force and virtue.

FIDELITY AND DEPOSIT
COMPANY OF MARYLAND
By ROBERT HECHT
Attorney in Fact

Attest:
[Seal] S. M. SMITH
Agent

State of California,
County of Los Angeles—ss.

On this 25th day of April, 1941, before me Theresa Fitzgibbons, a Notary Public, in and for the County and State aforesaid, duly commissioned and sworn, personally appeared Robert Hecht and S. M. Smith, known to me to be the persons whose names are subscribed to the foregoing instrument as the Attorney-in-Fact and Agent respectively of the Fidelity and Deposit Company of Maryland, and acknowledged to me that they subscribed the name of Fidelity and Deposit Company thereto as Prin-

cipal and their own names as Attorney-in-Fact and Agent, respectively.

[Seal] THERESA FITZGIBBONS

Notary Public in and for Los Angeles County, State of California.

My Commission Expires May 3, 1942.

[Endorsed]: Filed Apr. 28, 1941. [24]

[Title of District Court and Cause.]

CERTIFICATE OF CLERK

I, R. S. Zimmerman, Clerk of the District Court of the United States for the Southern District of California, do hereby certify that the foregoing pages numbered from 1 to 25 inclusive, contain full, true and correct copies of Petition for Writ of Habeas Corpus; Order for Writ; Writ of Habeas Corpus; Return to the Writ; Traverse to the Return; Minute of Decision; Memorandum and Order Discharging the Writ; Notice of Appeal; Statement of Points on Appeal; Stipulation and Order Re Original Immmigration Records; Stipulation and Order Re Printing; Designation of Record on Appeal; and Cost Bond on Appeal, which together with the Original Records of the Immigration and Naturalization Service transmitted herewith constitute the record on appeal to the United States Circuit Court of Appeals for the Ninth Circuit.

I do further certify that the fees of the Clerk for comparing, correcting and certifying the foregoing record amount to $4.70 and that the said amount has been paid to me by the Appellant.

Witness my hand and the seal of the District Court of the United States for the Southern District of California, this 16th day of May, A. D. 1941.

[Seal] R. S. ZIMMERMAN,
Clerk,
By: EDMUND L. SMITH
Deputy.

[Endorsed]: No. 9826. United States Circuit Court of Appeals for the Ninth Circuit. Gin Soon Ging, Appellant, vs. William A. Carmichael, District Director of Immigration and Naturalization Service, Appellee. Transcript of Record. Upon Appeal from the District Court of the United States for the Southern District of California, Central Division.

Filed May 17, 1941.

PAUL P. O'BRIEN,
Clerk of the United States Circuit Court of Appeals for the Ninth Circuit.

In the United States Circuit Court of Appeals
for the Ninth Circuit

No. 9826

GIN SOON GING,

Appellant,

vs.

WM. A. CARMICHAEL, District Director of Immigration and Naturalization,

Appellee.

STATEMENT OF POINTS ON WHICH APPELLANT INTENDS TO RELY ON THE APPEAL AND DESIGNATION OF NECESSARY PARTS OF RECORD FOR THE APPEAL.

STIPULATION

(Rule 19, Subdivision 6 of Circuit Court of Appeals in and for the Ninth Circuit.)

It is hereby stipulated by and between the parties hereto through their respective counsel pursuant to Rule 19, Subdivision 6 of the Rules of the Circuit Court of Appeals in and for the Ninth Circuit, that the Statement of Points and Designation of Parts of Record filed in the District Court on the 25th day of April, 1941, and each and every part thereof, shall be and is hereby designated as necessary for the consideration of the appeal herein.

Dated this 25th day of April, 1941, at Los Angeles, California.

Y. C. HONG
Attorney for the Appellant
WM. FLEET PALMER
United States Attorney
By ATTILIO DI GIROLAMO
Asst. United States Attorney
Attorneys for the Appellee

[Endorsed]: Filed May 17, 1941. Paul P. O'Brien, Clerk.

No. 9826

IN THE

United States Circuit Court of Appeals

FOR THE NINTH CIRCUIT

In the Matter of

GIN SOON GING,

On *Habeas Corpus.*

BRIEF OF APPELLEE.

WM. FLEET PALMER,
United States Attorney,

By RUSSELL K. LAMBEAU,
Assistant United States Attorney,

United States Post Office and Court House Building, Los Angeles,

Attorneys for Appellee.

Parker & Baird Company, Law Printers, Los Angeles.

TOPICAL INDEX.

TABLE OF AUTHORITIES CITED.

CASES.

STATUTES.

No. 9826

IN THE

United States Circuit Court of Appeals

FOR THE NINTH CIRCUIT

In the Matter of

GIN SOON GING,

On *Habeas Corpus.*

BRIEF OF APPELLEE.

Statement of the Case.

This is an appeal taken from an order of the District Court denying appellant's petition for a Writ of Habeas Corpus. [Tr. p. 13.] By stipulation and order [Tr. p. 18], certain original immigration and naturalization records have been filed with the clerk of this Court. These files comprise the entire record upon which the administrative finding and order under attack herein was made. Wherever the occasion arises these records will be referred to by their file numbers appearing on the jacket in the righthand corner, excepting the certified Department of Justice file No. 56040/574, which will be referred to as the "Immigration Record". This latter file contains a complete transcript of the hearing accorded Gin Soon Ging by the Board of Special Inquiry.

The appellant, Gin Soon Ging, hereinafter called the "applicant", was born in China and is of the Chinese race. He has never been in the United States. On June 30, 1940, he arrived at San Pedro, California, from China on the SS "President Cleveland" and sought admission to the United States as the foreign-born son of Gin Ting. The United States citizenship of Gin Ting is conceded by the immigration authorities and is not at issue here. The applicant's case was heard by a Board of Special Inquiry appointed under Section 17 of the Immigration Act of February 5, 1917 (8 U. S. C. A. 153). After hearing the testimony offered by the applicant and his witnesses, the Board of Special Inquiry determined the applicant had not established his claimed citizenship status and therefore unanimously voted to exclude him from the United States. From this decision the applicant appealed to the Attorney General. After a hearing by the Board of Immigration Appeals at Washington, D. C., the decision of the Board of Special Inquiry was affirmed and the appeal dismissed. Thereupon the applicant petitioned for a writ of habeas corpus. From an order denying the writ the applicant has appealed to this Court.

The Issue.

This case presents but one issue:

WAS THE APPLICANT ACCORDED A FAIR HEARING?

> "* * * If it does not affirmatively appear that the executive officers have acted in some unlawful or improper way and abused their discretion, their finding upon the question of citizenship must be deemed conclusive and is not subject to review by the court."
>
> *Tang Tun v. Edsell,* 223 U. S. 673, 675.

ARGUMENT.

The rules of law applicable to this case have long been clearly defined. In the case of:

> *Jung Sam v. Haff* (C. C. A. 9, decided December 18, 1940), 116 Fed. (2d) 384,

at page 387, the Court, speaking through Judge Garrecht, stated the principles controlling a review of these proceedings as follows:

> "It is established by a large number of decisions that 'the findings of the immigration officers on questions of fact affecting the right of an alien to enter this country are conclusive against any inquiry by the courts.' Fong Quong Hay v. Nagle, 9 Cir., 17 F. 2d 231, 232. Just as firmly fixed is the rule, in cases of this character, that before this court on review can overturn the determination of immigration authorities it must appear that the evidence submitted on the application for admission so conclusively established the fact in issue that the order of exclusion must be held arbitrary or capricious. Mui Sam Hun v. United States, 9 Cir., 78 F. 2d 612, 615. Denial of fair hearing is not established merely by proving the decision of the immigration officers was wrong. United States *ex rel.* Tisi v. Tod, 264 U. S. 131, 133, 44 S. Ct. 260, 68 L. Ed. 590; Kishan Singh v. Carr, 9 Cir., 88 F. 2d 672, 679. It is of no consequence that this court may have found differently than the immigration officers upon the evidence adduced, for it is not our function to weigh the evidence, but to consider whether or not the applicant was accorded a fair hearing. Mui Sam Hun v. United States, *supra;* Ong Guey Foon v. Blee, 9 Cir., 112 F. 2d 678, 689; Dong Ah Lon v. Proctor, 9 Cir., 110 F. 2d 808, 809, 810."

The applicant seeking admission to the United States has the burden of submitting satisfactory proof of his citizenship.

United States ex rel. Polymeris v. Trudell, 284 U. S. 279;

Quon Quon Poy v. Johnson, 273 U. S. 352;

Mui Sam Hun v. United States (C. C. A. 9), 78 F. (2d) 612;

Won Ying Loon v. Carr (C. C. A. 9), 108 F. (2d) 91, 92.

The applicant in the case at bar has never resided in the United States. He was born in China and is of the Chinese race. Under the treaty, laws and rules governing the admission of Chinese (22 Stat. L. 826; 58, 115, 476, 477:—28 Stat. L. 7; 32 Stat. L. 176) he is inadmissible unless he can satisfactorily establish that he is a citizen of the United States. He claims he is the legitimate foreign-born son of Gin Ting and that therefore he is a citizen of the United States under Section 1993, Revised Statutes. On this question the applicant, who had the burden of proof, offered no evidence except the oral testimony of himself, his alleged father, Gin Ting, and an unrelated witness, Gin Wing Fun. No documentary evidence of any kind was produced or offered to support the claimed relationship between the applicant and Gin Ting.

It was the duty and function of the immigration authorities to determine if the claimed parent-son relationship actually existed. This question of fact was decided ad-

versely to the applicant by a tribunal authorized by law to consider and decide such a question. Commenting upon this function of the Board of Special Inquiry in the recent case of

> *Young Nguey Sek v. Carmichael* (C. C. A. 9, decided March 11, 1941), 118 F. (2d) 105,

Circuit Judge Denman said:

> "* * * The Board and the Secretary of Labor had to decide no more than that appellant had failed in his burden to show *affirmatively* the parent-son relationship." (Emphasis ours.)

After hearing and weighing the testimony the Board of Special Inquiry, composed of three members, decided the applicant had failed to show affirmatively the parent-son relationship.

This case is a matter of identification involving citizenship. The only evidence presented on this issue was the oral testimony of the interested parties themselves, namely, the applicant and his alleged father, Gin Ting. The testimony of the witness Gin Wing Fun is of no value on this point. He is not related to the applicant and has no personal knowledge of the relationship between the applicant and Gin Ting. He merely testified that he had seen the applicant twice in China, once in 1937 and again in 1938. [Immigration Record, Q. 100-103.] But even in this there is a conflict. Seattle file 7032/2754 shows that when this witness returned from a trip to China June 15, 1938, he was asked under oath if he had visited the home in China

of any resident of the United States or if he had been introduced to the son, wife, or daughter of any resident of this country while in China, and he replied in the negative. When confronted with this contradictory prior testimony the witness attempted to explain this by saying that the interpreter told him it was not necessary to mention what village and who he had visited in China. It was not incumbent upon the Board to accept this explanation and it did not do so.

The testimony of the applicant and that of his alleged father was to the effect that applicant was born in the Fung Wah Village, China, C. R., 15-4-14 (May 25, 1926). [Hearing p. 26 and Immigration Record, Q. 76.] Gin Ting further testified that he had three sons born in China as follows [Q. 76]:

> "1. Gin Hung Guon—age 30, born Jan. 30 or 31, 1912, in Fung Wah Village, China.
>
> 2. Gin Soon Gan (applicant), age 15, born June 24 or 25, 1926, in Fung Wah Village, China, and
>
> 3. Gin Son Pang, age 14, born May 4 or 5, 1927, in Fung Wah Village."

The applicant, likewise, states his alleged father has three sons, as follows [Q. 8]:

> "1. Gin Hing Goon; married marriage name Gin Man Toy, age 30; I never asked my mother when he was born, so I don't know; he was married in our village, C. R. 22-12-20 (Feb. 3, 1933) to Wong Shee of Ngor May Village, Hoy Shan. He was born in our village. He has tried to come to America twice and has been deported twice * * *.

2. Myself.

3. Gin Soon Pang, age 14, born C. R. 16-5-15 (June 14, 1927) at our village and is now home attending the Que Gee School located about one or two li to the South of our village."

It is with respect to the alleged brother-son, Gin Hung Goon, that the most serious discrepancy in the testimony of the applicant and his alleged father appears. File No. 37221/7-27 relates to this alleged brother-son. It shows he twice sought admission to the United States as the son of Gin Ting and was twice rejected. Each time the alleged father Gin Ting appeared and gave testimony. But there were so many discrepancies between his testimony and that of the applicant on family matters and on the question of the age of the applicant that the claim of relationship was rejected. The court's attention is invited to the summary of the Board of Special Inquiry appearing in file 37221/7-27 [pp. 40-45]. The record also shows that a review of that decision was sought in the courts through habeas corpus proceedings but the petition was denied.

The applicant in the instant case now testifies he is the blood brother of Gin Hung Quon, and in so testifying he makes some of the same mistakes his alleged father made regarding this same Chinese. The present applicant identifies a photograph of said Gin Hung Quon as his brother. [Q. 13 and 14.] He testified that said Gin Hung Quon has one son named Gin Thloon Jom, born C. R. 24-6-13 (July 15, 1935) in the Fung Wah Village and that Gin Hung Quon never had any other children. [Q. 10, 11.]

The alleged father, when testifying on behalf of said Gin Hung Quon at San Francisco on August 13, 1937, testified as follows [San Francisco file 37221/7-27, p. 27]:

"Q. How many of your sons have been married? A. My oldest son, Gin Hung Quon.

Q. When, where and to whom was he married? A. I do not know when he was married. He was married in Hong Kong to Wong Shee.

Q. Can you state during what year he was married? A. It was either C. R. 22 or 23 (1933 or 1934). I received a letter from him telling me about it.

Q. Did you keep the letter referred to? A. No, I tore it up.

Q. Has applicant's wife borne him a child or children? A. *He wrote to me in the second letter stating he had a daughter; that is all. It was about a year after he was married that he sent me this second letter.*

Q. Did applicant Gin Hung Quon inform you what the name of his daughter was? A. *Gin Joon Shem.*

Q. Do you know where the wife and daughter of applicant now reside? A. They are now living at the Fung Wah Village." (Emphasis ours.)

And in the same proceeding, Gin Hung Quon himself testified on August 13, 1937, as follows [San Francisco file 37221/7-27, p. 17]:

"Q. How many times have you been married? A. Once only.

Q. When, where, and to whom were you married? A. In C. R. 23-12-12, changes, 23-12-20 (Jan. 24, 1935) to Wong Shee in Fung Wah Village.

Q. Has your wife borne you a child or children? A. No.

Q. Is she an expectant mother? A. I don't know."

Thus we have Gin Hung Quon testifying in 1937 that he had no children, Gin Ting testifying in the same year that Gin Hung Quon had a daughter, Gin Joon Shem, and the applicant in the case at bar testifying that Gin Hung Quon has a son, Gin Thloon Jom, born July 15, 1935.

Speaking of such contradictions in the case of

Won Ying Loon v. Carr, supra,

Circuit Judge Mathews said:

> "Whether in testifying as they did, appellant and Won Doo Mo (alleged father) were deliberately lying or were stating what they honestly believed to be true is, for present purposes, immaterial. Whatever their intentions or beliefs may have been, their testimony was partly, if not wholly, false. Knowing this, and not knowing which part, if any, of their testimony was true, the board was warranted in rejecting it all and holding that appellant's claim that he was Wong Ying Loon had not been established."

The Board of Special Inquiry unquestionably had a right to consider prior departmental records and to base its decision on the discrepancies developed through the use of such records:

Soo Hoo Yen v. Tillinghast (C. C. A. 1), 24 F. (2d) 163;

U. S. ex rel. Ng Kee Wong v. Corsi (C. C. A. 2), 65 F. (2d) 564;

Ex parte Wong Foo Gwong (C. C. A. 9), 50 F. (2d) 360;

Tang Tun v. Edsell, supra.

It is clear, therefore, that testimony of an alleged prior deported brother in conflict with the present applicant may properly be considered by the Board of Special Inquiry and form the basis of an excluding decision. And it has been held that where one applicant's claim is dubious, the claim of the others that he is their brother weakens their assertion:

> *Chung Fong Kwon et al. v. Tillinghast,* 33 F. (2d) 398 (affirmed 35 F. (2d) 1016).

But there is more than this fatal conflict in the testimony of the principal actors in the case at bar. In 1931 Gin Hong Quon, whom the applicant claims is his blood brother, testified that his father, Gin Ting, had been married twice and that he and all the other sons were issue of the second wife, Lee Shee. Both the present applicant and the alleged father have testified that the latter was married once.

Having in mind these contradictions in the testimony, it cannot be fairly said that the Board of Special Inquiry (the triers of the fact) acted capriciously in rejecting the claimed relationship. And, when considering further the fact that there has been no direct identification of the applicant as the son of Gin Ting, it cannot be fairly said that the applicant has sustained the burden of proof. Here the alleged father, Gin Ting, is in no position to identify the applicant as his son. He has not been in China since 1927 when the applicant was slightly over a year old. It is not unreasonable to refuse to accept his testimony under such circumstances. In the case of

Tillinghast v. Flynn ex rel. Chin King, 38 F. (2d) 5,

it was held that where the identifying witness had not seen the applicant since the latter was 5½ years old and the applicant was then 13 years, refusal to accept his testimony was not unreasonable.

Respondent submits that the administrative proceeding in the case at bar was fair in every respect and that there is ample justification for rejecting the applicant's claim.

Reply to Appellant's Brief.

Counsel complains that the Board was arbitrary in refusing to believe the testimony of the applicant because of the discrepancies developed and because the testimony of the applicant and his witnesses agreed in many details.

It is observed that counsel includes in his brief the statement of a certain Inspector Roy M. Porter, of Seattle (p. 15). This particular statement is not a citation from any case but a purported extract from a Department file, which presumably is a part of the Department records at Washington. It is not in evidence or alluded to by administrative officials in the case at bar. It is, of course, recognized that examination of arriving aliens vary in each particular case. This case is like many which involve the citizenship of Chinese applicants. The facts are wholly within the knowledge of interested witnesses, and fabrication can only be detected by the inconsistencies between their versions, or inherent contradictions, since the bare

narration is seldom antecedently improbable. The object of bringing out discrepancies is to impeach the witness or to give a ground for disbelieving him. There is no rule by which the seriousness of discrepancies can be measured. Each case depends upon its own facts.

White v. Chan Wy Sheung (C. C. A. 9), 270 F. 764;

Tom Ung Chai v. Burnett (C. C. A. 9), 25 F. (2d) 574;

Young Mew Song v. United States (C. C. A. 9), 36 F. (2d) 563;

Chan Nom Gee v. United States (C. C. A. 9), 57 F. (2d) 846.

In the case of

Hom Dong Wah v. Weedin, 24 F. (2d) 774,

this court quoted with approval from the opinion in the case of *Sui Say v. Nagle,* 295 F. 676, as follows:

> "In cases of this character, experience has demonstrated that the testimony of the parties in interest as to the mere fact of relationship, cannot be safely accepted or relied upon. Resort is therefore had to collateral facts for corroboration, or the reverse. If the witnesses are in accord as to a number of collateral facts which they should know if the claimed relationship exists, and probably would not know if the claim of relationship did not exist, there is at least a reasonable probability that the testimony is true. If, on the other hand, the witnesses disagree as to the collateral facts which they should or would know if the claimed relationship exists, especially such an important fact as membership in the immediate family of the parties, there is a strong probability that the claimed relationship is false and fraudulent."

Although there are details upon which the testimony agrees, as contended by counsel, it is not possible to reconcile the discrepancies hereinabove commented upon. On this point in the case of

> *Weedin v. Yee Wing Soon* (C. C. A. 9), 48 F. (2d) 36,

Circuit Judge Wilbur said:

> "In the case at bar, we have a multitude of agreements upon a great variety of details in the testimony which are quite consistent with the claimed relationship and point with great emphasis to the truth of the claim. On the other hand, we have a discrepancy that is difficult if not impossible to reconcile with the alleged relationship. * * *"

And, in further comment on this aspect of the case, said:

> "* * * At the outset it must be conceded that there is a complete accord in the testimony upon such a multitude of details as would hardly be expected if the claim of relationship did not exist. Indeed, such a complete accord would hardly be anticipated if the relationship did exist unless there was some previous conference between the witnesses to refresh their memory upon the numerous details upon which they might reasonably expect to be examined."

Counsel also attempts to apply rules of evidence to the proceedings before the Board of Special Inquiry; however, it is not open to the courts to consider either the admissibility or the weight of proof according to the ordinary rules of evidence, and the fact that the rules of evi-

dence as applied in courts of law are violated does not show that the hearing was unfair.

Healey v. Backus, 221 Fed. 358;
Frick v. Lewis, 195 Fed. 693;
Lee Lung v. Patterson, 186 U. S. 168, 176.

Appellee submits that the discrepancies developed in this case are sufficiently serious to preclude the determination that the applicant was not given a fair hearing or that the District Court erred in sustaining such finding. The record fully bears out District Judge Beaumont in his conclusion [Tr. p. 14] that:

> "After a study of the record herein the Court cannot say that the Board of Special Inquiry committed a manifest abuse of the power and discretion conferred upon it. In this case the evidence is such that reasonable men might differ as to its probative effect."

Conclusion.

For the reasons hereinabove stated, appellee respectfully submits that the lower court did not err in holding and finding that there was no manifest abuse of discretion by the immigration authorities, and that the administrative order was not a result of an arbitrary or unfair hearing. Wherefore, appellee prays that the decision of the lower court be affirmed and appeal dismissed.

Respectfully submitted,

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No. 9826.

IN THE

United States Circuit Court of Appeals

FOR THE NINTH CIRCUIT

GIN SOON GING,

Appellant,

vs.

WM. A. CARMICHAEL, District Director of Immigration and Naturalization,

Appellee.

BRIEF FOR APPELLANT.

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Pleadings.

This is an appeal from an order of the District Court dismissing the writ of habeas corpus previously issued upon the application of the appellant. The petition was made by appellant's father, Gin Ting, on September 25th, 1940 [Tr. of R. pp. 2-7], the writ was issued and served on the same day [Tr. of R. p. 8], the appellee's return to the writ attaching the Immigration records involved was filed on October 7, 1940 [Tr. of R. pp. 9-10], and traverse to the return was submitted in the appellant's behalf on October 10th, 1940 [Tr. of R. pp. 11-12]. Issue was thus joined.

Jurisdictional Statement.

Jurisdiction of the court below to review the proceedings of the Immigration Service was invoked by the appellant on the ground that he was denied a fair hearing of his case under the provisions of 28 U. S. C., Section 451

(R. S., Section 751). The present appeal is authorized by the provisions of 28 U. S. C., Section 225-a (Jud. Code, 128, as amended).

Facts of the Case.

Gin Soon Ging, the appellant, was a 14-year-old boy of the Chinese race who came to the port of San Pedro, California on June 30th, 1940 and applied to the Immigration authorities there for admission as a natural born American citizen by virtue of the provisions of Section 1993 of the Revised Statutes. He left China to join his American-born father, Gin Ting, in this country. As evidence of his citizenship, Gin Ting presented United States Citizen's Certificate of Identity No. 5888 issued to him by the Commissioner of Immigration and Naturalization at San Francisco, California on November 7th, 1911. Appellant claimed that he was born to the said Gin Ting and wife on May 25th, 1926 in China, and that he was therefore entitled to admission as the foreign-born son of a native-born American citizen under the aforesaid statute.

Appellant's application was heard by a board of special inquiry on July 9th, 1940. His alleged father, Gin Ting, and clansman, Gin Wing Fun, appeared before the board to testify in his behalf. After hearing the testimony of the appellant and his two witnesses on matters concerning his ancestors, parents, brothers and other relatives, the detailed description of his Chinese home, ancestral village and schooling as well as many other matters and events which the board believed the appellant and his alleged father should have common knowledge by virtue of their relationship to each other, no discrepancies or inconsistent statements were developed. The board nevertheless, denied the appellant the right of admission and based its exclud-

ing decision solely on the ground that there were some discrepancies between the testimony of his alleged father and Gin Hong Goon in certain Immigration proceedings had in 1931 and 1937 to which the appellant was not even a party. The board was also in receipt of an anonymous letter saying that the appellant was Gin Ting's grandson and not his son, so an additional finding to that effect was made for the appellant's exclusion.

Appeal was then taken to the Immigration Board of Review in Washington, D. C., that the hearing was unfair and findings were not supported by facts. The appellate board, however, dismissed the appeal and confirmed the excluding order of the trial board. Thereupon, a writ of habeas corpus was applied for by the appellant's father in his behalf to obtain judicial review of the same. This is an appeal from the order of the court below dismissing the writ.

Specifications of Error.

The court below held that the board of special inquiry did not commit a manifest abuse of the power and discretion conferred upon it and that the excluding decision rendered against the appellant was not reached unfairly or arbitrarily [Tr. of R. pp. 12-14]. Appellant believes the court below was in error. Specifications of error are expressed in his statement of points for appeal filed on April 25th, 1941 [Tr. of R. pp. 16-18].

The question at issue may therefore be succinctly stated as follows: *Was the hearing accorded the appellant by the Immigration Authorities arbitrary and unfair?* Appellant contends that he was denied the fair hearing to which he was entitled.

ARGUMENT.

I.

The Board of Special Inquiry Committed a Manifest Abuse of the Power and Discretion Conferred Upon It by Arbitrarily Rejecting the Uncontradicted Testimony of the Appellant's Alleged Father Concerning His Relationship to the Appellant.

There was not a single discrepancy developed between the testimony of the appellant and his alleged father before the board of special inquiry. The examination accorded them touched upon every detail pertaining to their ancestral history, family, relatives, home, village, and hundreds of various collateral events which took place during their lives. The pedigree reputation was also corroborated by the testimony of their clansman Gin Wing Fun. The board, however, arbitrarily brought into the picture certain discrepancies developed in 1931 and 1937 between the testimony given by the appellant's father and appellant's alleged brother, Gin Hung Goon, who failed to gain admission to this country, and sought thereby to discredit the appellant's father's present testimony.

Of course, the law's method of ascertaining the credibility of witnesses is nothing new and has been known for centuries. Aside from the appearance of the witness, his demeanor on the stand, the reasonableness of his testimony, and his character, he can only be impeached by evidence of contradictory statements made out of court or in another tribunal on material matters. *Gung You v.*

Nagle (C.C.A. 9th), 34 Fed. (2d) 848, 852. The matter material to appellant's case is the relationship between the appellant and his alleged father. Not only was there no disclaimer of such parentage by appellant's father in the 1931 and 1937 proceedings, the official records of those proceedings are replete with antecedent testimony by him concerning the birth and existence of the appellant in his family and home in China. There was, therefore, no valid ground for the board to reject either the present or previous testimony of the appellant's father pertaining to his relationship to the appellant. To do so is an unwarranted abuse of power and discretion.

On appeal to the appellate board in Washington, D. C., the language used in the decision rendered on September 18th, 1940, reads as follows:

> "The Board of Special Inquiry appears to have found the appellant's alleged father to be discredited as a witness by reason of the record fact that in 1931 and again in 1937 he testified in support of the claim of one Gin Hung Quon to be his son and, therefore, entitled to admission as a citizen, which claim was not found to be established with the result that the said Gin Hung Quon was returned to China at the conclusion of those two proceedings. *Reference to the records of those two applications, however, fails to show that fraud was proved or even alleged in either of them. Thus, it is not believed that the Board of Special Inquiry is warranted in finding the alleged father discredited by reason of his testifying in those proceedings.*" (Emphasis ours.)

II.

The Board of Special Inquiry Was Arbitrary and Unfair in Relying on the Questionable Contents of an Anonymous Letter to Base an Order of Exclusion Because the Rights and Privileges of Citizenship Cannot Be So Lightly Denied the Appellant.

Shortly previous to the supplementary hearing held on July 23rd, 1940, the board of special inquiry was in receipt of an anonymous communication to the effect that the appellant was Gin Ting's grandson and not his son as claimed. During the course of the hearing, appellant's father produced a family group photograph taken in China many years ago as additional evidence of relationship which was overlooked in the first hearing and in which appeared the appellant, his mother Lee Shee, his younger brother Gin Soon Pang, his older brother Gin Hung Goon and the latter's wife Wong Shee. After the unexpected introduction of this photograph, the board showed it to the appellant who without any hesitation identified and named each and every person therein. The board, however, paid lip service to the law as laid down by our Supreme Court in *Kwock Jan Fat v. White,* 253 U. S. 454, 40 S. Ct. 566, 64 L. Ed. 1010, by stating that the anonymous information was given "no credence" because of its source, came out with the wild stab in the dark by finding that the said photograph appeared to be that of a "father and mother and two children and a grandmother", which alleged opinion if it were based on fact, would furnish support to the allegation contained in the anonymous letter, and, of course, would make the appellant's mother his grandmother. This remarkable finding of the board may be characterized solely as a prejudicial effort to give full weight and credence to the anonymous infor-

mation whipsawing the evidence around to suit the convenience of the suspicion of the members of the board by making the wish the father to the thought. Even the Immigration Board of Appeals had to acknowledge the invalidity of such a ground on September 18, 1940, as follows:

> "Also, it appears that while the Board of Special Inquiry has given no credence to anonymous information that this appellant is a grandson instead of a son of his alleged father; yet, *that Board appears to have indirectly given some weight to that information in finding that the group photograph presented 'would appear to be the photograph of father and two children and a grandmother', which would accord with the anonymous information,* instead of being, as the alleged father and appellant testify, a picture of the appellant and his mother, and his older brother and the latter's wife, and his younger brother." (Emphasis ours.)

Under the same circumstances, this Honorable Court held in the case of *Chew Hoy Quong v. White* (C.C.A. 9th), 249 Fed. 869, 870, as follows:

> "Aside from that, we hold that the fact that the immigration authorities received a confidential communication concerning the applicant's right to admission, upon which they acted, and which was forwarded to the Department of Labor for its consideration, was *sufficient to constitute the hearing unfair.* However far the hearing on the application of an alien for admission into the United States may depart from what in judicial proceedings is deemed necessary to constitute due process of law, *there clearly is no warrant for basing decision, in whole or in part, on*

confidential communication, the source, motive, or contents of which are not disclosed to the applicant or her counsel, and where no opportunity is afforded them to cross-examine, or to offer testimony in rebuttal thereof, or even to know that such communication has been received." (Emphasis ours.)

See, also:

Wong Gook Chun v. Proctor (C.C.A. 9th), 84 Fed. (2d) 763.

III.

The Board of Special Inquiry Acted Most Arbitrarily and Unfairly by Disregarding Direct and Material Evidence on the Issue of Relationship Between the Appellant and His Alleged Father in Order to Render Its Decision of Exclusion.

By reason of the fact that Gin Ting had not been back to China since 1927 when the appellant was an infant two years old, the board of special inquiry disregarded the testimony in support of the claimed relationship. This Honorable Court in the case of *Gung You v. Nagle,* 34 Fed. (2d) 848, 852, said:

"Relationship is not usually proved by physical facts, and never is where the mother does not testify, but by pedigree reputation in the family, and by the conduct of the parties, including the manner in which they live. The fact that a small child lives in the home of its alleged parents and that they maintain toward each other the obligation involved in the relationship is evidence favorable to the issue, and evi-

dence that they did not live together and did not conduct themselves as parent and child is evidence to the contrary. *Such evidence is not collateral evidence; it is direct and material evidence on the issue.*" (Emphasis ours.)

The mere fact that the appellant's father has not seen the appellant in person since the latter was an infant therefore could not reasonably discredit his father's testimony on his conduct toward the appellant, or testimony of others on the pedigree reputation in their family. In 22 Corpus Juris 172, Section 103 g, the following passage is found, viz.:

"Relationship. The rule admitting declarations concerning pedigree applies to a question of relationship; in addition to which a person may testify as to his relationship to another person, especially where the statement is based on his own knowledge; and parentage may be proved by general reputation."

And in 22 Corpus Juris 173, Section 106 (3), the following is noted:

"Identity. In the absence of direct evidence by the conclusion of witnesses, or by inspection of the court and jury, *identity may be established circumstantially not only by proving extrinsic facts which render its existence probable, but by proof of indicative manifestations,* such as declarations showing peculiar knowledge, or by conduct, such as residence in a particular country, state, or other place, or service in the army at a certain time. *A family tradition may assist in identification, and hearsay statements in the nature of declarations regarding pedigree are competent for the same purpose.*" (Emphasis ours.)

It is readily seen that the law does not require physical identification of the appellant by his alleged father, who may or may not be able to recognize him in person as they have been separated from each other ever since the appellant was an infant, although in this particular case, the father was able to do so because of having kept in constant touch with his family during all these years and of having received pictures of the appellant from the boy's mother from time to time, one of which was contained in the family group photograph used as an exhibit herein and another attached to the affidavit of relationship. It was therefore arbitrary and unfair for the Immigration officials to disregard this unimpeached, direct, and material testimony given by the appellant's father on the relationship issue. This flagrant disregard of the principles of justice constituted a denial of due process of law.

In the court below, the appellee cited in this connection, the Massachusetts case of *Chung Fong Kwon v. Tillinghast,* 35 Fed. (2d) 398, and *Tillinghast v. Chin King,* 38 Fed. (2d) 5, neither of which has any application to the case at bar. The first one, a District Court case, refers to the failure of the applicant as a native born to produce a birth certificate showing his birth *in this country* where recording of such vital statistics is required by statute. There is no such a requirement in China. The second case refers to the testimony of the identifying witness who has not seen the applicant since he was five and a half years old and not to the testimony of the applicant's father. The identifying witness Gin Wing Fun in the case at bar, testified that he saw the appellant in China in August, 1937 and again in April, 1938 when the appellant was about 12 or 13 years of age [p. 11, Immigration board hearing of July 9, 1940].

IV.

The Appellant Having Satisfied His Burden of Proof by Establishing With Evidence to a Reasonable Certainty That He Was the Son of Gin Ting, the Board of Special Inquiry Was Arbitrary and Unfair in Excluding Him Without Some Substantial Evidence to the Contrary.

The American citizenship of appellant's alleged father Gin Ting was conceded by the board of special inquiry. His trip to China making possible his claim of paternity to the appellant was a matter of official record, San Francisco Immigration File No. 25882/4-4, showing that he departed from the United States on August 22, 1925 and returned from China on May 15th, 1938 when he reported to the Immigration Authorities that he had a son by the appellant's name was born to him and his wife on this trip. Thereafter, on each and every occasion of his several appearances before the Immigration Authorities at San Francisco, San Diego, Tucson and San Pedro, he reiterated the existence of a son by the appellant's name and age. This Honorable Court in *Louie Poy Hok v. Nagle*, 48 Fed. (2d) 753, 755, said:

> "A similar case arose in *Ng Yuk Ming v. Tillinghast,* 28 Fed. (2d) 547, 549 (C.C.A. 1st). There, '13 years before * * * *the alleged father* * * * *testified before the immigration authorities that he has a son bearing the name of the applicant,* * * * *which he confirmed on every other occasion upon which he was called to testify.*' The decision of the Court was that the decision of the immigration officials was not supported by the evidence and the prisoner was ordered released from custody. See, also, Gung You v. Nagle, 34 Fed. (2d) 848 (C.C.A. 9th). In the instant case the cumulative effect of the repeated

assertions by the father and the previously entered alleged brothers that there was a third son, Loue Fung Leung, born October 1, 1909, certainly go farther than a mere indication that the three were suffering from a delusion; the effect of the testimony in the mind of any reasonable man must be to create the belief that there was a third son somewhere in the offing." (Emphasis ours.)

Other cases holding the same view are: *U. S. ex rel. Lee Kin Toy v. Day,* 45 Fed. (2d) 206; *Johnson v. Ng Ling Fong,* 17 Fed. (2d) 11, 12; *U. S. ex rel. Leong Ding v. Brough,* 22 Fed. (2d) 926, 927; and *U. S. ex rel. Ng Gon Yuen v. Reimer,* 20 Fed. Supp. 976, 977.

The appellant and his father were given a most searching examination by the board of special inquiry at San Pedro. Appellant testified that his name was Gin Soon Ging; that he was born on May 25, 1926 in the Fung Wah Village, Gon Ung Bow section, Hoy-shan district in China; that he had resided in that Chinese village continuously since his birth up to the time of departure for the United States on this trip; that he was destined to his father, Gin Yan Oy, in Los Angeles; that his father's name was Gin Tan (Ting) and Gin Yan Oy was his father's marriage name; that his father was about 60 years of age and a cook by occupation; that his father was married only once, and that was to his mother, Lee Shee; that his mother Lee Shee was 56 years old and her birthday came on the 20th day of the 1st month each year; that his mother was a native of the Nom village, Hoy-shan district in China; that there were three boys in his family including himself; that the oldest boy in the family was Gin Hung Goon, who was about 30 years old and married

to Wong Shee from the Ngor May village in 1933, and they had one son named Gin Thloon Jon born in 1935; that he, the applicant, was the second child in the family; that his younger brother Gin Soon Pang, who was born to his parents in 1927, constituted the third member of his family; that his oldest brother Gin Hung Goon had made two attempts to gain admission into the United States, first time in 1931 and 1937, without any success; that his paternal grandfather was Gin San, or Gin Yat Gim by his marriage name, who died long ago and was buried in the Gai Gung How hill located about a third of a mile north of his home village; that his mother told him his grandfather was married twice—first to Fong Shee of Ung Nan village and after her death to another woman from the same clan and that his father was the son of his grandfather's first wife; that his grandmother and step-grandmother were buried with his grandfather in the aforesaid hill; that as these people died before his birth, he had never seen any of them; that his father had no brothers or sisters; and that his mother was the only child in her family. So much intimate knowledge of the family history the appellant had readily displayed and his alleged father under cross-examination corroborated the same in practically every detail.

As to his native village in China, the appellant testified that he lived in the 4th house on the 2nd row from the head of the Fung Wah village in China all his life up to May 10, 1940 when he left home for the United States; that the Fung Wah village consisted of 12 dwellings, 12 toilets or outhouses, and one school building; that the school-house is on the first row and there were three other rows of houses, each row thereof having four dwellings; that the houses on each row all adjoin each other; that

there was a fishpond in front of the village; that the villagers got their drinking water from a well located at the tail-end of the village close to the fishpond; and that the bamboo hedges at the rear and the two sides and the fishpond in front acted as protective barriers to the village. He made a diagram of the village for the enlightenment of the members of the board of special inquiry and the same was marked Exhibit "B" in the record.

With reference to his ancestral home, the house in which he was born and lived up to the present time, he described as follows:

> "It is a one story green brick house consisting of two bedrooms; two kitchens and one parlor. It has a tile roof and cement floor. There are two outside windows in each bedroom, one above and one below the loft and there are two inside windows between the bedrooms and the parlor. There is one skylight in each bedroom protected by glass and each bedroom has a cross-loft. There is a shrine loft in the parlor, there are two outside entrances, entering into the kitchens."

He further testified that his oldest brother, Gin Hung Goon's family shared this house with them; that his brother Goon occupied the big door side bedroom with his wife and son, while the appellant and his mother and youngest brother Pang slept in the small door side bedroom. His description of the home was used in the cross-examination of his alleged father and no discrepancies thereon could be developed. There could be no question that they shared a very thorough knowledge of the family residence in China.

As to out of ordinary events, the appellant testified that in CR 27 (1938) some bandits attacked his village and kidnapped his mother and oldest brother Gin Hung Goon and that they were later released only upon payment of a ransom. He also told about the unexpected visits by an old friend of his father's by the name of Gin Wing Fun from the United States in 1937 and 1938 bringing money as well as tidings of his father's good health across the ocean. Gin Wing Fun appeared before the board to verify this and identified the appellant as the boy whom his friend and clansman Gin Ting requested him to see when he got to China. Appellee in the court below sought to discredit this testimony because this matter was not contained in a certain questionnaire signed by this witness aboard the incoming steamer upon his return to this country at Seattle in June, 1938. The appellee should be quite familiar with the hasty methods used in filling these form reports when everything is done under pressure and time is very limited for checking and discharging passengers. In the case of *Chan Cheung,* Immigration Bureau No. 55702/44, Inspector Roy M. Porter of Seattle, a man of years of experience in such work, frankly admitted as follows:

> "However, it is known by all experienced officers that the statements taken from incoming Chinese on board the steamers are practically worthless so far as the real truth is concerned, as the *examining officers are hurried in their work and the Chinese persons examined have not the time necessary to think and recall when subjected to such questions in a hurried way. It is well known that nearly every Chinese who departs from the United States takes some letter or money from some friend in the United States to his family in China.*" (Emphasis ours.)

Therefore, it was not without reason for the court to hold in the case of *Flynn v. Tillinghast,* 32 Fed. (2d) 359, that *such alleged answers to a "stock omnibus question" form is a "very slight and insufficient ground on which to adjudge testimony unreliable."*

In reviewing the evidence, there was ample direct and material testimony in support of the relationship claimed by the appellant to his alleged father Gin Ting on the one hand, and not a scintilla of evidence to support the findings of the board of special inquiry to the contrary or to the effect that the appellant was a grandson instead of a son of Gin Ting on the other. Administrative tribunals may ascertain facts in any reasonable and fair manner they see fit, but they cannot reject sworn, consistent and unimpeached testimony without some real reasons which a fair-minded person would regard as adequate; *Ward v. Flynn ex rel. Yee Gim Lung,* 74 Fed. (2d) 145. The burden of proof was so satisfactorily met by the appellant that the board could not cite one material discrepancy between the testimony of the appellant and his father in the hearing. Our courts have repeatedly held that there must be at least some substantial evidence to support an excluding decision; *Nagle v. Wong Ngook Hong* (C.C.A. 9th), 27 Fed. (2d) 650; *Johnson v. Leung Fook Yung,* 16 Fed. (2d) 65; *Johnson v. Ng Ling Fong,* 17 Fed. (2d) 11; and *Leong Ding v. Brough,* 22 Fed. (2d) 926.

Our courts had long ago repudiated the theory that the Immigration Authorities have the power to reject the testimony of any number of apparently credible witnesses

and decide against them in favor of a presumption that an applicant is not an American citizen, but on the contrary, have time and time again restated the rule that *the testimony of one credible witness is sufficient in law to overcome that presumption; Gung You v. Nagle* (C.C.A. 9th), 34 Fed. (2d) 848, 852.

Conclusion.

This case certainly falls under the principle laid down by our Supreme Court in *Tisi v. Todd,* 264 U. S. 131, 44 S. Ct. 260, 63 L. Ed. 590, that the error of an administrative tribunal may be so flagrant as to render the hearing unfair. The uncontradicted evidence established conclusively the relationship of father and son between Gin Ting and the appellant and it was a manifest abuse of power and discretion for the Immigration Authorities to disregard the same without some substantial reason other than the questionable information contained in the anonymous communication. *Go Lun v. Nagle* (C.C.A. 9th), 22 Fed. (2d) 246; *Hom Chung v. Nagle* (C.C.A. 9th), 41 Fed. (2d) 126; *Nagle v. Jin Suey* (C.C.A. 9th), 41 Fed. (2d) 522; and *Gung You v. Nagle* (C.C.A. 9th), 34 Fed. (2d) 848.

It is well-settled that, when a claim of citizenship, which is more than colorable, is denied, the courts will scrutinize the administrative proceedings with great care to the end that American citizens shall not be unjustly deprived of

their citizenship; *Wong Hai Sing v. Nagle* (C.C.A. 9th), 47 Fed. (2d) 1021, 1024; *Woon Sun Seung v. Proctor* (C.C.A. 9th), 99 Fed. (2d) 285. Let us not forget our Supreme Court's admonition in *Kwock Jan Fat v. White,* 252 U. S. 454, 40 S. Ct. 566, 64 L. Ed. 1010, that:

> "It is better that many Chinese immigrants should be improperly admitted than one natural born citizen of the United States should be permanently excluded from his country."

It is therefore respectfully requested that the order of the court below in dismissing the writ be *reversed* with direction to discharge the appellant from the illegal custody of the Immigration Authorities.

Dated at Los Angeles, California, June 23rd, 1941.

Respectfully submitted,

You Chung Hong,
Attorney for Appellant.

No. 9847

United States

Circuit Court of Appeals

For the Ninth Circuit.

A. H. FAVOUR and A. G. BAKER,
Appellants,

vs.

HARRY W. HILL, Receiver of Intermountain Building and Loan Association,
Appellee.

Transcript of Record

Upon Appeal from the District Court of the United States for the District of Arizona.

PARKER PRINTING COMPANY, 545 SANSOME STREET, SAN FRANCISCO

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[Clerk's Note: When deemed likely to be of an important nature, errors or doubtful matters appearing in the original certified record are printed literally in italic; and, likewise, cancelled matter appearing in the original certified record is printed and cancelled herein accordingly. When possible, an omission from the text is indicated by printing in italic the two words between which the omission seems to occur.]

ATTORNEYS OF RECORD

FAVOUR, BAKER AND CRAWFORD,
Bank of Arizona Building,
Prescott, Arizona.
Attorneys for Appellants.

BAKER and WHITNEY,
LAWRENCE L. HOWE,
Luhrs Tower,
Phoenix, Arizona.
Attorneys for Appellee. [3*]

[Title of District Court and Cause.]

PORTIONS OF "RECEIVER'S PETITION FOR ORDER DETERMINING PREFERENCES AND PRIORITIES AMONG CREDITORS, SHAREHOLDERS AND INVESTORS; AND FOR ORDER TO SHOW CAUSE THEREON", THAT RELATE TO CLAIM OF FAVOUR & BAKER, AS SHOWN ON PAGES 7 AND 8 OF SAID PETITION:

* * * * * * *

That on or about the 18th day of April, 1934, one Margaret Cobb recovered a purported judgment against the Association in the Superior Court of the State of Arizona, in and for the County of

*Page numbering appearing at foot of page of original certified Transcript of Record.

Yavapai, for the sum of $1,000.00, with interest thereon at 6% per annum from January 1, 1934, until paid, together with court costs in the further sum of $38.61. That upon obtaining said purported judgment the said Margaret Cobb took out special execution in aid thereof and the Sheriff of Yavapai County purported to sell an asset of the Association at sheriff's sale. That at said sheriff's sale and on April 30, 1934, the property of the Association so offered for sale was purportedly sold to one R. O. Barrett for $1,064.06 in full payment and satisfaction of the judgment and costs, and thereupon satisfaction of said judgment was duly entered of record. That the law firm of Favour & Baker, composed of A. H. Favour and A. G. Baker, thereafter purported to purchase from R. O. Barrett the property the latter had acquired at said sheriff's sale. That the said firm of Favour & Baker are now asserting as against the Association such rights as Margaret Cobb had against the Association, if any, by reason of her original judgment. That the said claim and demand of Favour & Baker is hereby rejected and disallowed in its entirety.

[Endorsed]: Receiver's Petition for Order Determining Preferences and Priorities, etc. Filed Jul. 23, 1940. Edward W. Scruggs, Clerk, United States District Court for the District of Arizona. By Wm. H. Loveless, Chief Deputy Clerk. [4]

[Title of District Court and Cause.]

ORDER OF REFERENCE

Receiver's Petition for Allowance and Disallowance of claims and to Determine Preferences and Priorities, if any, among and between creditors, investors, shareholders and others, having come on regularly for hearing on the 16th day of September, 1940, and good cause appearing therefor, and the issues involved thereon being voluminous, upon consideration thereof and the Court being fully advised in the premises,

It Is Ordered that said Petition and any and all claims against the Intermountain Building & Loan Association be referred to Neil C. Clark, Esquire, Heard Building, Phoenix, Arizona, as a Special Master in Chancery herein for hearing and determination, said Special Master to take evidence and proofs according to law; to examine the questions in issue thereon and to report from said evidence and proofs his findings of fact and conclusions of law in respect to each of said claims in these proceedings, and report his conclusions as to whether or not said claims should be allowed as against the Intermountain Building and Loan Association, the priorities and the amounts thereof.

It Is Further Ordered that said Special Master shall make a report to the Court of his action in the premises and shall give notice to all persons whose claims are presented to him of the filing of such report and shall advise them that excep-

tions thereto must be filed with the Clerk of this Court within ten (10) days from the filing of his report.

It Is Further Ordered that with respect to the matters herein referred to said Special Master he shall have all the powers conferred upon a Master by Rule 53 of the Federal Rules of Civil Procedure.

Dated at Phoenix, Arizona, this 16th day of September, 1940.

DAVE W. LING
Judge [5]

[Endorsed]: Filed Sep 16 1940 Edward W. Scruggs, Clerk United States District Court for the District of Arizona By Gwen J. Ballard, Deputy Clerk. [6]

[Title of District Court and Cause.]

PORTIONS OF "REPORT OF SPECIAL MASTER" THAT RELATE TO NOTICE GIVEN BY THE SPECIAL MASTER TO CREDITORS, AS SHOWN ON PAGES 1 AND 2 OF SAID REPORT.

To the Judges of the District Court of the United States, for the District of Arizona:

Comes now Neil C. Clark, as Special Master appointed by interlocutory decree entered herein on the 16th day of September, 1940, and respectfully reports as follows:

That on the 23rd day of July, 1940, Mr. Harry W. Hill, as Receiver of the Intermountain Building & Loan Association filed herein his report of the claims of creditors, investors, shareholders, and others, aggregating approximately 3012 claimants against the Association, and with said report filed a petition praying for an order of this Court for the allowance or disallowance of each of the several claims filed and a determination of the preferences and priorities, if any, among the creditors, investors, shareholders and others; and it appearing that the issues were involved and voluminous, it was ordered that said petition be referred to the undersigned as a Special Master in Chancery, to hear evidence in reference to said claims, and to examine the questions in issue arising from said petition, and to report his findings of fact and conclusions of law in respect to each of said claims, and whether or not said claims should be allowed, and the priority, if any, and amount of each of said claims.

On the 16th day of September, 1940, the undersigned was duly sworn to the faithful performance of his duties as Special Master and filed his oath in the office of the Clerk of this Court. Thereafter the undersigned fixed Thursday, October 3, 1940, at 10:00 o'clock a. m., at 124 North First Avenue, Phoenix, Arizona, as the [7] time and place for the first hearing under said order of reference, and caused notice of said hearing to be published in the Phoenix Gazette, a newspaper of general

circulation in the County of Maricopa, State of Arizona, published at Phoenix, Arizona, on the 28th day of September, 1940, and also caused a similar notice to be published on the 29th day of September in the Arizona Republic, likewise a newspaper of general circulation in the State of Arizona, proof of publication of which is hereto attached; and in addition thereto, written notice of said hearing was personally served upon Thomas W. Nealon and E. G. Monaghan, as attorneys for plaintiff herein, and others similarly situated, and said notice was sent by registered mail to each investor in contracts and securities of the Association whose claims were based upon contracts or certificates not bearing the security clause hereinafter mentioned; notice of said hearing also appeared in the news columns of the newspapers above mentioned and many other newspapers published in the states wherein the Association had actively engaged in business and where a great majority of the creditors of the Association now reside.

[Endorsed]: Report of Special Master Filed Dec 14 1940 Edward W. Scruggs, Clerk United States District Court for the District of Arizona. By Gwen J. Ballard, Deputy Clerk. [8]

[Title of District Court and Cause.]

MOTION THAT MASTER APPROVE JUDGMENT CLAIM OF A. H. FAVOUR AND A. G. BAKER; EXCEPTIONS TO REPORT OF RECEIVER; MOTION FOR SUBSTITUTION OF EXECUTORS.

Come now the above named claimants, pursuant to order of the Court dated September 16th, 1940, referring claims to a Special Master, and respectfully move and except as follows:

I.

This claim is based upon a judgment for One Thousand Dollars ($1000.00), obtained by Margaret Cobb against the Intermountain Building & Loan Association in Cause No. 12971 in the Superior Court of Yavapai County, Arizona, on April 18th, 1934, before appointment of the Receiver herein, as said judgment was finally corrected and amended by order of February 28th, 1939. The judgment and order are attached to and made a part of the claim filed herein.

The judgment of April 18th, 1934, foreclosed a purported attachment of a mortgage in which the Intermountain Association was mortgagee, and a purported sale of the constructively attached property was made to R. O. Barrett, and a purported satisfaction returned by the Sheriff. The Arizona Supreme Court held void the attachment and sale, but not the judgment establishing the debt. in a later action (lower Court No. 13722) in which the Receiver and these claimants as assignees of the

judgment in favor of Margaret Cobb and R. O. Barrett, were parties. The Superior Court thereupon corrected the judgment in Cause No. 12971 to conform to the said decision of the Supreme Court, and eliminated the attachment and sale and all other proceedings thereafter, as null and void, leaving the judgment valid as establishing the debt. Margaret Cobb and R. O. Barrett thereafter again assigned to A. H. Favour and A. G. Baker, the claimants herein, the judgment as corrected; and their claim was filed, based upon said judgment establishing the debt.

II.

The Receiver, in his report filed herein, disallowing [9] the claim subject to such order as may be made by the Court, appears to base his rejection upon that part of the record (since held void) in said Cobb case, which shows the sale (now void) to R. O. Barrett and the consequent satisfaction (now void). The Receiver is unaware of, or does not take into consideration, the record since the void satisfaction. This later record sets aside the execution and all proceedings thereafter as void. The said Margaret Cobb did, on May 17th, 1934, make written assignment to R. O. Barrett of the judgment of April 18th, 1934, and in said assignment she states "said judgment debt and costs with interest thereon are still owing" to her, and she covenants that "the said judgment is in full force and effect and that the whole of the said sum of One Thousand Dol-

lars ($1,000.00) with interest and costs remains owing thereunder".

III.

This is a claim established as aforesaid by a judgment in the case in which the said defendant appeared and answered, and before a receiver was appointed. Neither the Intermountain Association nor the Receiver has paid any part thereof to any person at any time entitled to receive payment. No property of said defendant or the Receiver has been received by any person. The purported sale of the mortgage was set aside as void, and the defendant and the Receiver remained in possession of said mortgage as mortgagee, with full title thereto. Equity requires that the claim be approved with other judgment claims of its class.

Wherefore, these claimants respectfully move and pray that the Special Master:

First: Approve said judgment claim after such notice and hearing as may be accorded to creditor claimants;

Second: That said claim be given the preference allowed judgments in such cases.

Third: That Eva Favour, as Executrix, and Arthur G. Baker, as Executor, of the Estate of A. H. Favour, Deceased, be [10] substituted in the place and stead of the said A. H. Favour, now deceased, as one of the claimants herein.

FAVOUR, BAKER &
CRAWFORD
By A. G. BAKER
Attorneys for Claimants.

State of Arizona,
County of Yavapai—ss.

A. G. Baker, being first duly sworn, on oath, deposes and says:

That he is one of the attorneys for the Claimants making the above motions and exceptions, and is also one of said Claimants; that he has read the foregoing instrument and knows the contents thereof, and that the same is true in substance and in fact.

A. G. BAKER

Subscribed and sworn to before me this 25th day of September, A. D. 1940.

My commission expires September 7th, 1943.

[Seal] VERA VOGE
Notary Public.

[Endorsed]: Filed Sep 27 1940 Edward W. Scruggs, Clerk United States District Court for the District of Arizona By Gwen J. Ballard Deputy Clerk. [11]

[Title of District Court and Cause.]

PORTION OF "REPORT OF SPECIAL MASTER" THAT RELATES TO CLAIM OF FAVOUR & BAKER. REPORT FILED DECEMBER 14th, 1940.

Judgment Creditors. (Page 41)

24. Claim of Favour & Baker. A. H. Favour and A. G. Baker have filed a claim for $1,038.61

with interest at the rate of 6% from January 1, 1934, until paid. This claim is based upon a judgment obtained under the following circumstances: Mrs. Margaret Cobb, living in Yavapai County, Arizona, during the month of January, 1934, commenced an action against the Intermountain Building & Loan Association to enforce the payment of a matured certificate for $1,000.00. Upon the commencement of the action the plaintiff caused a writ of attachment to be issued pursuant to which the Sheriff, in the manner hereinafter described, levied upon a mortgage of record in Yavapai County, given by Thomas Short and Catherina Short, his wife, as mortgagors, to the Intermountain Building & Loan Association as mortgagees. The levy, as shown by the Sheriff's return, was made in the following manner: "By serving a copy of said writ of attachment upon Thomas Short and Catherina Short, his wife, mortgagors; and that he caused a copy of said writ of attachment to be served upon the Intermountain Building & Loan Association, a Corporation, defendant, Mortgagee, and by causing a copy of this writ to be recorded in the office of the County Recorder of Yavapai County, Arizona."

[12]

Thereafter, on the 18th day of April, 1934, judgment was entered for the plaintiff as prayed for in the plaintiff's complaint, and further provided that: "The attachment heretofore made in this action upon all right of defendant in and to the real mortgage from Thomas Short and wife to de-

fendant in and to the real mortgage from Thomas Short and wife to defendant and recorded in Book 64 of Mortgages, page 153, in the office of the County Recorder, Yavapai County, be, and the same is hereby foreclosed, and that said attached property be sold on special execution in accordance with law and practice of this court." Thereupon an execution was issued and delivered to the Sheriff of Yavapai County, pursuant to which the following proceedings were had as shown by the Sheriff's return:

> "Under, and by virtue of the foregoing Execution and Order of Sale, R. M. Robbins, Sheriff of Yavapai County, duly seized and levied upon all property described in said Execution and Order of Sale in the manner and form required by law. I duly noticed said property for sale in satisfaction of said judgment, as required by law, and the mandate of said writ, by posting three printed copies of said notice in said county, as required by law, one copy of said notice being posted at the door of the Court House of said County, all for twenty-one days next before said sale.
>
> "On the 30th day of April, 1934, at the hour of 10 o'clock A. M., at the door of the Court House in said County, in the City of Prescott, all of said property mentioned, set forth and fully described in said Execution and Order of Sale, was duly offered for sale at public auction,

[13] in satisfaction of said judgment, pursuant to said notice and said writ. And at said sale all of the said property so described therein was duly struck off and sold to R. O. Barrett for the sum of Ten Hundred Sixty-four and 06/100 ($1064.06) Dollars, he being the highest bidder, and that being the highest sum bid, and said sum so bid, and received being equal to the judgment and costs in this case, this Execution and Order of Sale is now returned fully satisfied.

"I have made and delivered to the said purchaser the legal certificate of sale, and have filed for record with the County Recorder of said county, a true copy or duplicate of said certificate.

"The receipt of plaintiff's attorney in full satisfaction of said judgment is attached hereto and made a part of this return.

"Dated this 30th day of April, A. D. 1934.

R. M. ROBBINS,
Sheriff.
By. ROBT. V. BORN,
Deputy Sheriff."

That attached to the Sheriff's return was the original receipt of Favour and Baker, attorneys for plaintiff, referred to in the writ of which the following is a copy:

"Received of R. M. Robbins, Sheriff of Yavapai County, Arizona, the sum of Ten Hun-

dred Sixty-four and 06/100 ($1064.06) Dollars in full payment and satisfaction of the judgment and costs in the foregoing Execution and Order of Sale, said sum being the amount [14] bid and received for the property this day sold at Sheriff's sale in satisfaction of said judgment, and said sum so bid and received for the property this day sold at Sheriff's sale in satisfaction of said judgment, and said sum so bid and received being evidenced and represented by the Certificate of Sale issued to the purchaser of said property.

Dated this 30th day of April, A. D. 1934.

Judgment	$1,000.00
Interest	20.00
Attorney's fees	.....
Taxes	.....
Costs	38.61
Costs Accruing	5.45
Total	1,064.06
By Sale	1,064.06
Balance Due	.....

Signed: FAVOUR & BAKER
Attorneys for Plaintiff"

On the 17th day of May, 1934 (i. e., seventeen days after the Sheriff's sale), Mrs. Margaret Cobb, as plaintiff and judgment creditor in cause No. 12971, executed, acknowledged, and delivered to R. O. Bar-

rett an instrument purporting to be an assignment of the judgment, in which, among other things, she recited:

> "Now, therefore, this assignment of judgment, Witnesseth: That in consideration of the sum of $10.00 and other valuable considerations to Mrs. Margaret Cobb, now paid by R. O. Barrett, receipt whereof is hereby acknowledged, the said Mrs. Margaret Cobb hereby assigns to the said R. O. Barrett all the benefit and the advantage of the said judgment with interest thereon, the costs and all moneys recoverable under the said judgment to hold the same to the said R. O. Barrett absolutely in the foregoing form to-wit: [15] $1,000.00 with interest and costs and the said Mrs. Margaret Cobb hereby covenants with the said R. O. Barrett that the said judgment is in full force and effect and that the whole of said sum of $1,000.00 with interest and costs remains owing thereunder. In witness whereof, Mrs. Margaret Cobb has hereunder set her hand the 17th day of May, 1934."

That on or about the 30th day of April, 1934, for the consideration of $1064.06, R. O. Barrett executed and delivered his written assignment of the Margaret Cobb judgment to A. H. Favour and A. G. Baker.

Thereafter, on June 2, 1936, Thomas Short and Catherina Short commenced an interpleader action

in the Superior Court of Yavapai County, naming R. O. Barrett, A. H. Favour, A. G. Baker, and H. S. McCluskey, the Receiver of the Association, and the Association, as conflicting claimants of the note and mortgage, and praying that they be compelled to interplead and litigate their several claims among themselves. Thereafter the issues were tried and a judgment entered, in which the trial court found that the note and mortgage levied upon under the attachment in the Margaret Cobb suit belonged to Favour & Baker, as the assignees of R. O. Barrett, the purchaser at the Sheriff's sale.

An appeal was taken from this judgment to the Supreme Court of Arizona, and on November 28, 1938, the judgment was reversed. In its decision the Supreme Court held that the trial court exceeded its power in declaring that the attachment levy on the mortgage gave the plaintiff a lien on it or on the realty covered by it, for the reason that the procedure to procure the lien was sanctioned neither by the common law nor by statute, and that the order foreclosing the lien and sale were null and void and of no effect. [16]

Thereafter, in February, 1939, A. H. Favour and A. G. Baker, as assignees of the judgment of Mrs. Margaret Cobb in Cause No. 12971, petitioned the Superior Court in which the case was tried for an order in accordance with Section 3854, Revised Code of Arizona, 1928, directing that the record be made to conform to the decision of the Supreme

Court of November 28, 1938. The petition was granted, and the Superior Court on September 28, 1939, entered the following order:

> "The decision of November 28, 1938, of the Supreme Court, on appeal in Cause No. 13722 in this Court, having held that the foreclosure of attachment in the judgment in this cause dated April 18, 1934, was void, and the proceedings taken under said foreclosure being therefore void and of no effect, it is ordered pursuant to the authority of Section 3854 that the record be, and the same is hereby corrected herein to conform to said decision, and all proceedings, and the record of all proceedings, subsequent to the judgment of April 18, 1934, including the special execution and all proceedings and acts therein, thereunder, and thereafter taken or done, are and are hereby declared void by and under said decision of the Supreme Court, and are of no force or effect; the judgment of April 18, 1934, to otherwise remain in effect except as so modified or changed by said decision of November 28, 1938, of the Supreme Court of Arizona." [17]

The contract upon which the judgment of Margaret Cobb is based was entered into by and between Margaret Cobb and the Intermountain Building & Loan Association under which Margaret Cobb paid to the Association the sum of $693.00 in one hun-

dred twenty-six installments of $5.50, with the express understanding and agreement that when all of said instalments had been paid in full the Association would pay to her the sum of $1,000.00. When the certificate matured the Association refused or was unable to pay the amount due, but did agree that after claims filed previous to that of Margaret Cobb had been paid, and when sufficient funds were available for that purpose, the claim of Margaret Cobb would be paid. This arrangement not being satisfactory to Mrs. Cobb, she commenced the action above mentioned and the contract upon which her claim was based was converted into the judgment of April 18, 1934.

By reason of the proceedings herein described the Association has paid nothing to Margaret Cobb or any assignee of hers on account of the certificate and the Receiver has refused to allow the claim on the judgment, for the reason that it appears to have been satisfied by the Sheriff's sale held pursuant to the execution issued on the judgment of Margaret Cobb. It further appears that R. O. Barrett received from Favour & Baker an amount equal to the sum he paid to the Sheriff for the Sheriff's certificate of sale, later declared by the Supreme Court to be void." (Page 47) [18]

Conclusions of Law:

XVI. (Page 62)

The action of the Receiver rejecting the claim of Messrs. Favour and Baker as assignees of the

judgment obtained by Margaret Cobb against the Intermountain Building & Loan Association in the Superior Court of Yavapai County, Arizona, on the 18th day of April, 1934, is approved.

In view of the fact that this claim has been the subject of considerable litigation and its proponents have been diligent in presenting their objections to the Receiver's ruling, it is only fair that the Master's reasons for sustaining the Receiver should be briefly stated. Favour & Baker, as the assignees of Margaret Cobb, have exactly the same rights that she assigned to R. O. Barrett, and that he in turn assigned to Messrs. Favour & Baker. If Margaret Cobb, assuming she had made no assignment, is entitled to recover from the Association, so are Favour & Baker, her *assigness.* If she could not recover, neither can her assignees.

The judgment secured by Margaret Cobb against the Association on the 18th day of April, 1934, was valid insofar as it established her right to recover from the Association the amount she sued for. During the pendency of the action a writ of attachment was issued under which the sheriff attempted to levy upon a mortgage given by residents of Yavapai County on property in Yavapai County, to secure an indebtedness of the mortgagors to the Intermountain Building & Loan [119] Association. The judgment directed that the attachment lien on the mortgage be foreclosed. Pursuant to the judgment, a special execution was issued directing the Sheriff to sell the attached mortgage. This the Sheriff ac-

cordingly proceeded to do. The sale, after due notice, was held on the 30th day of April. The highest and best bid was that of R. O. Barrett for $1064.06. Barrett paid the amount of his bid to the Sheriff in cash. The Sheriff thereupon paid the money over to the attorneys for Margaret Cobb, and took from them a receipt which recited that the money was received and accepted in full payment and satisfaction of the judgment. Later the Supreme Court of Arizona held that the Sheriff's levy on the mortgage under the writ of attachment was a nullity; and that the judgment order foreclosing the attachment lien was void, and that the special execution and sheriff's sale and certificate of sale were likewise void. Even though the certificate of sale that the Sheriff delivered to Barrett was worthless and the proceedings upon which it was based were void, the Sheriff nevertheless received for it $1064.06, and this sum the Sheriff paid to Margaret Cobb's attorneys and they received it in full payment and satisfaction of the judgment. It is not necessary that an execution issue, or that there be a valid sale in order to satisfy a judgment. If the judgment creditor is paid in full, the judgment is satisfied. Margaret Cobb was paid in full on April 30, 1934, since which time she has had no claim against [20] the Association. Seventeen days later Margaret Cobb made an assignment to R. O. Barrett of "all benefit and the advantage of the said judgment * * * and all moneys recoverable under the judgment". Evidently Margaret Cobb had much faith in the durability and

virtue of her judgment, but it is a faith that we do not share. She had nothing to assign, and her assignees acquired nothing. One could feel considerable sympathy for Mr. Barrett, save for the fact that he sold whatever he acquired by Mrs. Cobb's assignment to Messrs. Favour & Baker for a consideration equal to the amount he paid the Sheriff for the impotent certificate of sale. It is obvious that Messrs. Favour & Baker have provided the money that satisfied their client's judgment, with the result that the Association has been relieved of a corresponding liability without cost, other than the expense incidental to protracted litigation. It may well be that Messrs. Favour & Baker, on some theory, have a just claim against the Association for reimbursement. It must rest, however, on something other than the vitality of the judgment of Margaret Cobb." (Page 65). [21]

[Endorsed]: Report of Special Master. Filed Dec. 14, 1940. Edward W. Scruggs, Clerk, United States District Court for the District of Arizona. By Gwen J. Ballard, Deputy Clerk. [22]

[Title of District Court and Cause.]

EXCEPTIONS TO REJECTION BY SPECIAL MASTER OF CLAIM OF A. H. FAVOUR AND A. G. BAKER

Come now the above named claimants, by their attorneys, and upon the following, and such other, grounds as may be presented at the hearing, except

to that part of the Report of the Special Master, filed December 14th, 1940, which rejects their claim for $1064.06, or any part thereof, although the Special Master in so rejecting states in substance that these claimants may well have a just claim against the Intermountain Building & Loan Association:

1. The disallowance of the claim upon the ground that the return of the Sheriff indicating satisfaction stands as conclusive even when the sale is declared void, would be erroneous and contrary to equity and decisions, for the reason that when a sale is void, any satisfaction based thereon is also void; and the record which has been submitted with this claim shows that the execution, sale, and all proceedings thereafter, including the apparent satisfaction in the Cobb case, were declared void by the Supreme Court and an order conforming thereto was entered by the trial Court. Any satisfaction based upon such void proceedings would likewise be void. There was, in law, no levy, no sale, and no satisfaction; hence the debt is still due.

2. The disallowance of the claim by the Court will result in injustice and inequity, for the reason [23] that, as reported by the Special Master, the Intermountain was paid in full for the Certificate, and no payment whatsoever has ever been returned by said Association to Margaret Cobb, the payor, or to any person for her, or to her assigns, these claimants, who paid to Margaret Cobb the full sum of $1064.06 for the assignment of her judgment and claim and interest to them, and who are the losers and real parties in interest.

The Special Master, in his Report, recognizes that these claimants have a just claim for reimbursement on some basis, and these claimants pray that this Court do equity in accordance with said recognition and as the case so admittedly calls for.

FAVOUR, BAKER & CRAWFORD,
By ALPHEUS L. FAVOUR,
Attorneys for Claimants.

State of Arizona,
County of Yavapai—ss.

A. G. Baker, being first duly sworn, deposes and says:

That he is one of the claimants above named; that he has read the foregoing Exceptions, and that the matters stated therein are, to his knowledge or in his belief, true in substance and in fact.

A. G. BAKER

Subscribed and sworn to before me this 23rd day of December, A. D. 1940.

[Seal] VERA VOGE,
Notary Public.

My Commission expires September 7th, 1943. [24]

[Endorsed]: Filed Dec. 26, 1940. Edward W. Scruggs, Clerk, United States District Court for the District of Arizona. By Wm. H. Loveless, Chief Deputy Clerk. [25]

In the United States District Court
for the District of Arizona

October 1940 Term At Phoenix

MINUTE ENTRY OF
MONDAY, JANUARY 20, 1941
(Phoenix Division)

Honorable Dave W. Ling, United States District Judge, Presiding

E-268

GUADALUPE R. GALLEGOS, et al,
Plaintiffs,

vs.

INTERMOUNTAIN BUILDING & LOAN ASSOCIATION, a corporation,
Defendant.

This case comes on regularly before the Court this day for hearing on the Report of Special Master and Exceptions to Report of Special Master filed by A. H. Favour and A. G. Baker, and by Mathilda J. Forst.

The Receiver, Harry W. Hill, is present with his counsel, Lawrence L. Howe, Esquire. Thomas W. Nealon, Esquire, and Charles Rawlins, Esquire, are present in their own behalf. J. H. Morrison, Esquire, appears as counsel for creditor, Southwestern Fire Insurance Company. E. O. Phlegar, Esquire, appears as counsel for claimant, Mathilda J. Forst, Alpheus L. Favour, Esquire, and A. G.

Baker, Esquire, appear as counsel for Claimants A. H. Favour and A. G. Baker. Ralph Stewart, Esquire, appears as counsel for the Ancillary Receiver in Utah. M. L. Ollerton, Esquire, appears as counsel for certain certificate holders in Utah and moves for continuance of this hearing to permit exceptions to be filed on behalf of said certificate holders, and

It Is Ordered that said motion be, and it is denied.

The said exceptions of A. H. Favour and A. G. Baker are now duly argued by respective counsel, submitted, and by the Court taken under advisement.

Said exceptions of Mathilda J. Forst are now submitted on briefs and by the Court taken under advisement. [26]

Ralph Stewart, Esquire, now makes statement to the Court on behalf of the Ancillary Receiver in Utah and

It Is Ordered that said Report of Special Master be submitted and by the Court taken under advisement. [27]

[Title of District Court and Cause.]

ORDER

This cause came on to be heard upon exceptions to the master's report filed therein, and was argued by counsel, and thereupon, upon consideration

thereof, it is Ordered, Adjudged and Decreed, as follows:

1. The exceptions of Mathilda J. Forst and A. H. Favour and A. *S.* Baker are overruled.

2. The special master, Paragraph IX, page 57 of his report, recommends that in the distribution of the assets of defendant, certificate owners who have borrowed from the Association, and pledged their certificates as security, be allowed the adjusted value as an offset against their indebtedness, and that they be paid as other creditors on any credit balance.

Owing to the high regard for the master's ability as a lawyer, it is with diffidence I hold that this view does not commend itself to the Court, First, because apparently the Association was insolvent, even from its inception. Secondly, because the Association, having been incorporated under the laws of Utah, it would appear that the law of that State should control in determining the relative rights of borrowing and non-borrowing certificate-holders. Both of the foregoing conclusions are supported by ample authority.

The receiver, therefore, will disregard the master's suggestion and will make distribution in accordance with the Utah statute which disallows offsets of the character under discussion.

Except as indicated, the report of the special master hereby is confirmed and approved.

Dated at Phoenix, Arizona, this 30th day of January, 1941.

DAVE W. LING
Judge [28]

[Endorsed]: Filed Jan. 30, 1941. Edward W. Scruggs, Clerk, United States District Court for the District of Arizona. By Gwen J. Ballard, Deputy Clerk. [29]

[Title of District Court and Cause.]

PETITION OF CLAIMANTS, A. H. FAVOUR AND A. G. BAKER FOR REHEARING

Come now A. H. Favour and A. G. Baker, claimants whose claim was rejected, and petition the Court to set aside that portion of the order of January 30th, 1941 herein, which overrules the exceptions of A. H. Favour and A. G. Baker to the report of the Master which denied their claim, and to re-open the case as it affects this claim, upon the following grounds, to wit:

I.

No specific findings were made on disputed matters arising on the objections and exceptions of these claimants to the Master's report, and claimants cannot tell upon what points or findings the Court based its order overruling the exceptions, as is required by practice and the decisions on such cases.

2. That the Property Settlement Agreement changed the status of income earned by Petitioner subsequent to the date thereof from community earnings to separate earnings of Petitioner.

III.

Assignment of Errors.

In making its decisions, as aforesaid, the United States Board of Tax Appeals committed the following errors upon which your Petitioner relies as the basis of this proceeding:

1. The Board of Tax Appeals erred in holding that the income of Petitioner from his personal services for that part of the year 1936 commencing September 1 and ending December 31, and his income from his personal services for that part of the year 1937 commencing January 1 and ending October 1, was taxable entirely to Petitioner as his sole and separate property.

2. The Board of Tax Appeals erred in holding that the Property Settlement Agreement entered into by Petitioner and his then wife, Gertrude Martha Somerville, had the effect of changing the status of his subsequent earnings from community earnings to separate earnings.

Wherefore, your Petitioner prays that this Honorable Court may review the decision and order of the United States Board of Tax Appeals and reverse and set aside the same, and direct the said Board of Tax Appeals to hold and determine that the income of Petitioner for all of the year 1936

and that part of the year 1937 commencing January 1 and ending October 1 was community property of Petitioner and his then wife, Gertrude Martha Somerville, taxable one-half to each of said parties; and for the entry of further orders and direc- [22] tions as shall be deemed meet and proper in accordance with law.

EDWARD L. CONROY
DON CONROY
Attorneys for Petitioner
501 Taft Building
Los Angeles, California

State of California,
County of Los Angeles—ss.

Edward L. Conroy, being duly sworn, says:

I am one of the attorneys for the Petitioner in this proceeding. I prepared the foregoing petition and I am familiar with the contents thereof. The allegations of fact contained therein are true to the best of my knowledge, information and belief. This Petition is not filed for the purpose of delay, and I believe that the Petitioner is fully entitled to the relief sought.

EDWARD L. CONROY

Subscribed and sworn to before me this 29 day of May, 1941.

H. G. LYMAN
Notary Public in and for said County and State.

[Endorsed]: U. S. B. T. A. Filed June 3, 1941.

[23]

[Title of Board and Cause.]

To:

Commissioner of Internal Revenue,
Internal Revenue Building,
Washington, D. C.

J. P. Wenchel, Attorney for Respondent,
Chief Counsel, Bureau of Internal Revenue,
Internal Revenue Building,
Washington, D. C.

You are Hereby Notified that on the 3rd day of June, 1941, a Petition for Review by the United States Circuit Court of Appeals for the Ninth Circuit of the decision of the United States Board of Tax Appeals, heretofore rendered in the above entitled cause, was filed with the Clerk of the Board. A copy of the Petition as filed is attached hereto and served upon you.

Dated: June 2, 1941.

EDWARD L. CONROY
DON CONROY
Attorneys for Petitioner
501 Taft Building
Los Angeles, California [24]

Service of the foregoing Notice of Filing and of a copy of the Petition for Review is hereby acknowledged this 3rd day of June, 1941.

J. P. WENCHEL
Chief Counsel
Bureau of Internal Revenue
Attorney for Respondent

[Endorsed]: U. S. B. T. A. Filed June 3, 1941. [25]

[Title of Board and Cause.]

STATEMENT OF EVIDENCE

The above entitled cause came on for hearing at Los Angeles, California, before the Honorable Eugene Black, a member of the United States Board of Tax Appeals, on the 10th day of June, 1940, Edward L. Conroy, Esq., appearing on behalf of Petitioner, and E. A. Tonjes, Esq., appearing on behalf of Respondent.

Thereupon the parties, by their respective attorneys, filed with the Board a written Stipulation theretofore entered into by their counsel, and the cause was submitted upon the facts set forth in said Stipulation. By said Stipulation the parties agreed:

That Petitioner and Gertrude Martha Somerville were husband and wife for several years prior to 1936 and on September 28, 1936, an Interlocutory Judgment of Divorce was entered in the Superior Court of the State of California, in and for the County of [26] Los Angeles, in which proceedings Gertrude Martha Somerville was plaintiff and Petitioner was defendant, and a true copy of said Interlocutory Judgment of Divorce is attached to said Stipulation, marked Exhibit "A" and by such reference made a part thereof; that on October 2, 1937, a Final Judgment of Divorce was entered in said divorce proceedings between Petitioner and his said wife, Gertrude Martha Somerville, and a true copy of said Final Judgment of Divorce is attached to

Master rejecting said claim. These claimants, Favour & Baker, appeal from the denial of the petition for rehearing filed by these appellants on [33] February 6th, 1941, and overruled on February 17th, 1941, and from any intermediate order necessarily affecting the final rejection of said claim.

FAVOUR, BAKER & CRAWFORD,
By A. G. BAKER,
Attorneys for Appellants,
A. H. Favour and A. G. Baker.
The Bank of Arizona Building,
Prescott, Arizona.

[Endorsed]: Filed Apr. 14, 1941. Edward W. Scruggs, Clerk, United States District Court for the District of Arizona. By Gwen J. Ballard, Deputy Clerk. [34]

[Title of District Court and Cause.]

BOND FOR COSTS ON APPEAL

Know All Men by These Presents:

That we, Favour & Baker, by A. G. Baker, and A. G. Baker, as Principals, and Globe Indemnity Company, a Corporation, as Surety, are held and firmly bound unto Harry W. Hill, Receiver of Intermountain & Loan Association, in the sum of Two Hundred Fifty Dollars ($250.00), to be paid to the said Harry W. Hill, Receiver, and his successors and assigns, for which payment, we bind ourselves, and our heirs, executors, administrators, successors and assigns, jointly and severally.

Signed and executed this 10th day of April, A. D. 1941. [35]

Whereas, on January 30th, 1941, in the above entitled Court and cause, final order was rendered against the said A. H. Favour and A. G. Baker, claimants, and on February 17th, 1941, petition for rehearing was denied, and said claimants have duly filed notice of appeal therefrom.

Now, the condition of this obligation is such that if the said claimants shall prosecute said appeal with effect and pay all costs if the appeal is dismissed or the order or judgment affirmed, or such costs as the appellate court may award, if the order or judgment is modified, then this obligation to be void; otherwise to remain in full force and effect.

FAVOUR & BAKER, and A. G. BAKER,
By A. G. BAKER,
Principals.

[Seal] GLOBE INDEMNITY COMPANY,
By P. G. PRITCHARD,
Surety.

[Endorsed]: Filed Apr. 14, 1941. Edward W. Scruggs, Clerk, United States District Court for the District of Arizona. By Gwen J. Ballard, Deputy Clerk. [36]

[Title of District Court and Cause.]

DESIGNATION OF PORTIONS OF RECORD TO BE CONTAINED IN RECORD ON APPEAL

Appellants designate the following portions of the record in this action to be contained in the record on appeal from rejection of their claim:

1. Notice of Appeal.
2. Statement of Points on which Appellants intend to rely.
3. This designation.
4. Portion of "Report of Special Master" relating to Judgment Claim of Favour & Baker (pages 41 to 47) and Conclusions of Law (page 62). Filed December 14, 1940.
5. Exceptions to Rejection by Special Master in his Report of the claim of Favour & Baker. Filed December 26, 1940.
6. Order of Court of January 30, 1941, overruling Exceptions and confirming Report of Special Master.
7. Petition for Rehearing of Favour & Baker. Filed February 7, 1941.
8. Order of Court denying Petition for Rehearing, made February 17, 1941.

(The appeal is that the findings of facts do not support the conclusion of law that the claim was satisfied by the sheriff's sale, afterwards held void. The only essential record under Rule 75 (e) consists of the findings and conclusions of the Special Master and the proceedings thereafter. The record prior

to his Report does not appear essential under the Rules requiring brevity, but the following portions are included as perhaps proper and useful)

9. Minute Order of September 16, 1940, referring claims to the Special Master.

10. Notice given by Special Master to Creditors, following said Order, of reference of claims to him and providing for written objections by mail to disallowance by Receiver.

11. Claim of Favour & Baker so referred to Special Master by Court Order, and reported to the Court in said "Report of Special Master." [37]

12. Motion that Master Approve Judgment Claim of Favour & Baker, Exceptions to Report of Receiver. Filed September 27, 1940.

13. Bond on Appeal.

FAVOUR, BAKER & CRAWFORD,
By A. G. BAKER,
Attorneys for Appellants.
A. H. FAVOUR and A. G. BAKER,
The Bank of Arizona Building,
Prescott, Arizona.

Dated April 16, 1941. [38]

[Title of District Court and Cause.]

STATEMENT OF POINTS ON WHICH APPELLANTS INTEND TO RELY

The appellants, in accordance with the requirement where the whole record of a case is not nec-

essary, state that the points upon which they intend to rely on the appeal, as is shown by and may be determined from the record, are as follows:

1. There is no dispute on the facts. The Special Master found them in his report, which the Court confirmed; and appellants accept these as conclusive. The ground of appeal is that the conclusion of law and decision rejecting the claim filed with the Receiver is erroneous.

These facts show that originally Cobb held a fully paid $1,000.00 certificate in the Intermountain Association. In 1934, before appointment of a receiver, Cobb brought suit in the State Court to enforce payment. A mortgage in which Intermountain Association was mortgagee was attached. Judgment was rendered for Cobb and for foreclosure of the attachment. On the sale Barrett bought. The return of the Sheriff showed the usual receipt signed in satisfaction. Favour & Baker later bought from Barrett for the full sum. Later, in another suit the Arizona Supreme Court held the attachment void, thus returning to Intermountain the property that had been bought on the sale. Favour & Baker then filed claim with this Receiver, based on the said judgment establishing the amount due. They claimed as assignees subrogated to the right to receive the debt due from Intermountain which had received full payment and had parted with nothing. The Special Master points this out; he states that the Receiver refused to allow the

claim "for the reason that it appears to have been satisfied by the Sheriff's sale". [39]

This conclusion of law was adopted by the Court, and by the Special Master, although the latter indicated that the claimants might have a just claim. It is from the conclusion of law, that the claim was satisfied by the Sheriff's sale, that appellants appeal, and further assign as errors of the lower Court:

2. The Court erred, upon the facts found by the Special Master, in confirming, over objection, his conclusions of law and decision, and in rendering judgment rejecting the claim.

3. The facts found by the Special Master are not sufficient to support the final order of the Court of January 30th, 1941, confirming his conclusion of law that the claim was satisfied by reason of the Sheriff's sale and return, and approving his rejection of the claim; and said order is contrary to the facts found.

FAVOUR, BAKER &
CRAWFORD,
By A. G. BAKER
Attorneys for Appellants,
A. H. Favour and A. G. Baker.
The Bank of Arizona Building,
Prescott, Arizona.

[Endorsed]: Filed Apr. 17, 1941. Edward W. Scruggs, Clerk, United States District Court for the District of Arizona. By Gwen J. Ballard, Deputy Clerk. [40]

[Title of District Court and Cause.]

AFFIDAVIT OF MAILING

State of Arizona,
County of Yavapai—ss.

A. G. Baker, being first duly sworn, on oath, deposes and says:

That on April 16th, 1941, true and correct copies of "Designation of Portion of Record to be Contained in Record on Appeal", and "Statement of Points on Which Appellants Intend to Rely," in the above entitled cause, were mailed at the United States Post Office, in Prescott, Arizona, to Messrs. Baker & Whitney, the attorneys for the Receiver, Harry W. Hill, in said cause; that said copies were enclosed in an envelope, and the envelope was sealed; that said envelope was addressed to said attorneys at their office address, to-wit: Luhrs Tower, Phoenix, Arizona; and that the postage thereon was fully prepaid.

A. G. BAKER

Subscribed and sworn to before me this 30th day of April, A. D. 1941.

[Seal] VERA VOGE
Notary Public

My commission expires September 7th, 1943. [41]

[Endorsed]: Filed May 1, 1941. Edward W. Scruggs, Clerk, United States District Court for the District of Arizona. By Gwen J. Ballard, Deputy Clerk. [42]

APPELLANTS' SUPPLEMENTAL DESIGNATION

Law Offices of
Favour, Baker & Crawford
Prescott, Arizona

June 3, 1941.

Alpheus H. Favour, 1880-1939
Arthur G. Baker
Albert M. Crawford
Alpheus L. Favour
Mr. Edward W. Scruggs, Clerk
U. S. District Court, Phoenix, Arizona

Dear Sir:

E-268 Phx. Gallegos v Intermountain

Replying to your letter of May 27th, we have been looking up the situation where for some reason the Clerk cannot send up some part of matters that may be part of the record on appeal. From what we have found it would seem that where *where* some document which the clerk is directed by rule to include, or some paper designated by appellant, cannot be sent, the clerk may state the nature of the omitted part and that it cannot be sent.

So it would be our suggestion that in place where item 10, the notice of Special Master, would come, you might state substantially:

1. The appellants, as No. 10 in their Designation of portions of the Record, request the inclusion of the Notice Given by the Special Master to

Creditors, providing for written objections by mail to disallowances by the Receiver.

This request cannot be complied with for the reason that a form of such Notice was never filed by the Special Master on this Office. However, the Report of said Master filed herein, states the following method and manner in which notice was given:

(Then insert quotation you mention on page 2).

2. The appellants as No. 11 in their said Designation, request the inclusion of the Claim of Favour & Baker, so referred to the Special Master by Court Order, and reported to the Court in the Report of Special Master, a part of this record.

This request cannot be complied with because [43] the claim is not on file in this Office, for the reason that the Court Order of May 22, 1936, and later orders enlarging the time for filing of claims, directs that claims be filed with the Receiver. However, the Receiver in his petition to the Court to determine preferences and priorities states the following on the claim:

(Then insert quote you mention as on pp. 7 & 8).

We do not believe these items are necessary; however, the appellate court might think differently, and if they are included in our Designation, and you give the reason for not being able to comply, the appellate court can, as we read the rules and decisions, order them up if necessary.

Your method of certification appears to comply with Rule 75 (g).

Thanking you,

We remain,

Respectfully yours,

FAVOUR, BAKER &
CRAWFORD

AGB

[Endorsed]: Filed Jun. 4, 1941. Edward W. Scruggs, Clerk, United States District Court for the District of Arizona. By Gwen J. Ballard, Deputy Clerk. [44]

In the United States District Court
for the District of Arizona

CLERK'S CERTIFICATE TO TRANSCRIPT OF RECORD

United States of America
District of Arizona—ss.

I, Edward W. Scruggs, Clerk of the United States District Court for the District of Arizona, do hereby certify that I am the custodian of the records, papers and files of said Court, including the records, papers and files in the case of Guadalupe R. Gallegos, et al, plaintiffs, versus Intermountain Building and Loan Association, a corporation, defendant, numbered E-268 Phoenix, on the docket of said Court.

I further certify that the attached pages, numbered 1 to 44, inclusive, contain a full, true and

correct transcript of the proceedings in said cause, and all the papers filed therein, together with the endorsements of filing thereon, called for and designated in Appellants' Designation of Portions of Record to be Contained in Record on Appeal, and Appellants' Supplemental Designation, filed in said cause and made a part of the transcript attached hereto, as the same appear from the originals of record and on file in my office as such Clerk, in the City of Phoenix, State and District aforesaid, with the exception of items numbered 10 and 11 referred to in said Designation, being Notice Given by Special Master to Creditors, and Claim of Favour & Baker, which are not included in said transcript for the reason that I fail to find the same among the papers filed in my office.

I further certify that the Clerk's fee for preparing and certifying to this said transcript of record amounts to the sum of $6.00 and that said sum has been paid to me by counsel for the appellants.

Witness my hand and the seal of said Court this 9th day of June, 1941.

[Seal] EDWARD W. SCRUGGS,
Clerk
By WM. H. LOVELESS
Chief Deputy Clerk. [45]

[Endorsed]: No. 9847. United States Circuit Court of Appeals for the Ninth Circuit. A. H. Favour and A. G. Baker, Appellants, vs. Harry W. Hill, Receiver of Intermountain Building and Loan Association, Appellee. Transcript of Record. Upon Appeal from the District Court of the United States for the District of Arizona.

Filed June 18, 1941.

PAUL P. O'BRIEN,

Clerk of the United States Circuit Court of Appeals for the Ninth Circuit.

In the United States Circuit Court of Appeals for the Ninth Circuit

No. 9847

A. H. FAVOUR and A. G. BAKER,

Appellants,

vs.

HARRY W. HILL, RECEIVER OF INTERMOUNTAIN BUILDING & LOAN ASSOCIATION,

Appellee.

STATEMENT OF POINTS ON WHICH APPELLANTS INTEND TO RELY

Come now the Appellants, and state that they hereby adopt as their points on appeal the state-

ment of points on appeal appearing in the transcript of record in this case.

Dated this 23rd day of June, 1941.

FAVOUR, BAKER &
CRAWFORD
Attorneys for Appellants.

[Title of Circuit Court of Appeals and Cause.]

AFFIDAVIT OF SERVICE OF STATEMENT OF POINTS ON WHICH APPELLANTS INTEND TO RELY.

State of Arizona,
County of Yavapai—ss.

A. G. Baker, being first duly sworn, on oath, deposes and says:

That on the 23rd day of June, 1941, he mailed a copy of "Statement of Points on Which Appellants Intend to Rely", in the above entitled matter, to Messrs. Baker & Whitney, Attorneys at Law, Luhrs Tower, Phoenix, Arizona; that said copy was placed in a sealed envelope, addressed as above, with postage thereon fully prepaid.

A. G. BAKER

Subscribed and sworn to before me this 23rd day of June, 1941.

[Seal] VERA VOGE
Notary Public.

My commission expires September 7th, 1943.

[Endorsed]: Filed June 25, 1941. Paul P. O'Brien, Clerk.

[Title of Circuit Court of Appeals and Cause.]

DESIGNATION OF RECORD FOR PRINTING

Come now the Appellants and designate for printing the entire transcript, except any formal portions or rearrangement for printing that the Clerk may change or require under the rules and custom.

Dated this 23rd day of June, 1941.

FAVOUR, BAKER &
CRAWFORD
Attorneys for Appellants.

[Title of Circuit Court of Appeals and Cause.]

AFFIDAVIT OF SERVICE OF DESIGNATION OF RECORD FOR PRINTING

State of Arizona,
County of Yavapai—ss.

A. G. Baker, being first duly sworn, on oath, deposes and says:

That on the 23rd day of June, 1941, he mailed a copy of "Designation of Record for Printing", in the above entitled matter, to Messrs. Baker & Whitney, Attorneys at Law, Luhrs Tower, Phoenix, Arizona; that said copy was placed in a sealed envelope, addressed as above, with postage thereon fully prepaid.

A. G. BAKER

Subscribed and sworn to before me this 23rd day of June, 1941.

[Seal] VERA VOGE
Notary Public.

My commission expires September 7th, 1943.

[Endorsed]: Filed June 25, 1941. Paul P. O'Brien, Clerk.

NO. 9847

United States
Circuit Court of Appeals
For the Ninth Circuit

A. H. FAVOUR and A. G. BAKER,

Appellants,

vs.

HARRY W. HILL, Receiver of Intermountain Building and Loan Association,

Appellee.

Opening Brief of Appellants

FAVOUR, BAKER & CRAWFORD,

A. G. Baker,
A. M. Crawford,
A. L. Favour.

The Bank of Arizona Building,
Prescott, Arizona

Attorneys for Appellants.

PRESCOTT COURIER

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Appellee.

Opening Brief of Appellants

INTRODUCTION

This is an appeal from the denial by the United States District Court, Arizona, of a judgment creditor's claim filed by the appellants as subrogees and assignees with the Receiver, appellee. The claim had been established by judgment in the State Court for $1,000.00 and costs against the Intermountain Association before appointment of the Receiver in

the United States Court. The Receiver disallowed it, on the ground it had been satisfied by sheriff sale, later held void. (T. R. 18). The District Court referred it and other objections to a Special Master on September 16, 1940. The Special Master found the undisputed facts, and concluded, although recognizing an inequity, that the claim must be rejected, because the sheriff's return showed payment in full by the purchaser of attached property, at execution sale upon the said judgment, notwithstanding that the sale was afterwards declared void, and the property, a mortgage, was restored to the Intermountain. The purchaser and appellants, assignees and also entitled by right of subrogation, have never received anything for the money paid. And the Intermountain and the Receiver have not paid the debt owed by them. The District Court overruled exceptions and confirmed the Report of the Special Master. The appeal was taken upon the ground that the facts found do not support the conclusion of law that a purported satisfaction under a void sale satisfies the unpaid debt of the Intermountain Receiver.

STATEMENT OF JURISDICTION

Jurisdiction of the United States District Court for the District of Arizona.

The jurisdiction of the District Court in the main case of Gallegos v. Intermountain, and in the juris-

diction to appoint the Receiver, is recognized by this Court in

Intermountain v. Gallegos (*CCA 9th*), 78 *Fed.* (2*d*) 972, *Certiorari denied in* 296, *U. S.* 80 *L. Ed.* 454.

These appellants, in accordance with notice given by the Receiver filed their judgment claim. The proceedings on this claim were ancillary to the main suit and the Court, having established jurisdiction in the main suit and receivership, had jurisdiction to act on this and other claims:

Carpenter v. Nor. Pac. R. Co., 75 *Fed.* 850. *U. S. Code, Title* 28, *Par.* 125; *Judicial Code, Sec.* 66.

Jurisdiction of the United States Circuit Court of Appeals.

This appeal is brought to review the final decision of the District Court in the Receivership proceedings, rejecting the said claim of appellants:

Jud. Code, Sec. 128 (*A*) *First, amended. Land Title and Trust Co. v. Asphalt Co.* (*CCA 3rd*), 127 *Fed.* 9.

On this case appeal was from an order of the District Court dismissing petition by a claimant. A Receiver had reported against allowance of the claim and the District Court confirmed the Report. The appellate Court reviewed the case.

Atlantic Trust Co. v. Dana (*CCA 8th*), 128 *Fed.* 217.

St. Louis Trust Co. v. Riley (*CCA 8th*), 70 *Fed.* 32.

STATEMENT OF PLEADINGS

About February 28, 1939, appellants, pursuant to notice, filed with the Receiver claim for $1,064.06, the amount established by judgment obtained by Margaret Cobb, predecessor in interest of appellants, against the Intermountain Association. The Receiver disallowed the claim and the Court referred it and objections to a Special Master. (T. R. 3).

Pursuant to notice given by the Special Master, appellants served and mailed their verified Motion That the Master Approve the Judgment Claim, with memorandum of authorities (T. R. 7). No answer was filed by the Receiver. The ground of the Motion was, as set out in the Introduction above, that the Receiver erred in concluding that the sheriff's return on a void sale constituted a final and unalterable satisfaction which excused payment of the debt.

While recognizing the inequity, the Special Master in his report stated his conclusion of law to be that the satisfaction entered on the void sale nevertheless satisfied the claim, (T. R. 20), and the Receiver should not pay this debt.

Exceptions to this rejection by the Special Master were filed by appellants and, after a hearing, the Exceptions were overruled. (T. R. 21-26). A petition for Rehearing was filed and overruled. (T. R. 27 and 30).

The sole ground of this appeal is that the facts found by the Special Master and adopted by the

Court do not support the Conclusion of Law that the return of satisfaction, made upon the void sale, satisfied the judgment claim of appellants as subrogees and absolved the Receiver from payment of the debt of the Intermountain Association. And the only pleadings or records necessary for the purpose of this review are the Report of Special Master (T. R. 10) and the Exceptions and proceedings thereafter.

STATEMENT OF FACTS

All the essential facts are found and stated in the Report of Special Master (T. R. 10) and approved and confirmed by the Court. (T. R. 26). They are briefly:

Prior to January, 1934, Margaret Cobb had a matured certificate for $1000 in the Intermountain Association, (T. R. 11 and 18) having paid all instalments; but she could not get payment. She brought suit against the Association in that month in the Superior Court of Yavapai County, Arizona. Defendant appeared and answered, and after trial, judgment was entered for her on April 18, 1934, (T. R. 18) prior to appointment of Receiver of the Intermountain in the Federal Court. The plaintiff had at the time of bringing suit had an attachment levied on a recorded mortgage in which the Association was mortgagee and Thomas Short and wife were mortgagors. (T. R. 11). The judgment foreclosed

the attachment, execution issued April 18, 1934, and at the execution sale R. O. Barrett purchased (T. R. 12), a statute of Arizona providing that levy may be made on any interest in property, legal or equitable. The sheriff's return of sale showed payment in full. (T. R. 13). Cobb, in addition, gave Barrett a written assignment of the judgment and of all her interest. (T. R. 15). They both thereafter gave similar assignments to Favour and Baker, who paid the full amount of $1064.06. (T. R. 19 and 21).

Later the Receiver, denying the validity of the attachment demanded payment from Shorts and they interpleaded the Receiver and these appellants in the Superior Court (T. R. 16). The lower court upheld the original Cobb judgment and sale. The Receiver appealed and the Arizona Supreme Court held that attachment of a mortgage could not be made and held void the execution and sale, (T. R. 16), thereby restoring to the Receiver all rights in the mortgage; the Court stated, however, that the judgment establishing the debt was "unimpeachable" (Hill v. Favour, 84 Pac. (2nd) 589). (T. R. 19). After this decision the Superior Court, in February, 1939, corrected the judgment and record to set aside as void the attachment, execution and sale, in conformity with that opinion. (T. R. 16).

The appellants then promptly filed within the time permitted their claim based upon the Cobb

judgment as it converted the claim and established the debt and the amount. (T. R. 18). This was filed with the Receiver as directed, in this United States Court case, as a judgment creditor claim.

The Receiver, as set out in the Statement of Pleadings above, filed report in or about July, 1940, rejecting the claim, as having been satisfied by the sheriff's return on the void sale. (T. R. 1). The Court referred it to a Special Master. Written notice was mailed by the Special Master that any persons having objections to the Receiver's disallowance might appear or in lieu of a personal appearance such persons might submit their written objections or a statement of their contentions by mail. Appellants accordingly mailed their Motion That Master Approve the Claim (T. R. 7). In addition appearance was later made before the Master with the Receiver represented, and offer was made by appellants to confirm by documentary or other testimony the statements in the sworn Statements, if the Master considered any necessary. But there was no dispute of the facts, and the Report of the Master found the undisputed facts. Exceptions were filed by appellants to the conclusion of law of the Master that the satisfaction entered on the void sale satisfied the claim (T. R. 20). The Court overruled the exceptions and confirmed the Report.

ABSTRACT OF THE CASE

The Court, as above mentioned, overruled appellants' exceptions to the conclusion of law in the Report of the Special Master, and approved and confirmed the Facts and Conclusions therein as his own. So the only issue on the appeal is whether, based upon the Facts found by the Master, the satisfaction reported on a void sale is notwithstanding the invalidity a conclusive satisfaction of this claim and of the unpaid debt of the Receiver; that is, does this conclusion of law follow from the undisputed facts.

Appellee appears to stand on the proposition that if a satisfaction is returned by a sheriff, it is conclusive, and the fact the sale was void, or any other evidence to show it is erroneous and ineqitable, cannot be considered; and the judgment debtor can thus avoid payment of his debt. No authorities have ever yet been cited by appellee to support his contention.

Appellants stand on the proposition that on the undisputed facts here, the satisfaction which was entered upon the sale, afterwards declared void, is also void; and as the judgment debtor or its Receiver had the property, never in fact sold, restored to him, he still owes the debt and cannot claim such a satisfaction discharges him. We stand on this appeal upon the words quoted by the United States Supreme Court in Davis v. Gaines, 104 U. S. 386, that nothing could be more unjust than to permit a debtor to

recover back his property because the sale is irregular, and yet allow him to profit thereby to discharge his debt.

SPECIFICATION OF ERROR No. 1:

The Court erred in overruling (T. R. 25) appellants exceptions and in confirming that part of the Report of Special Master in which he concluded as a matter of law upon the facts found, that this judgment claim was conclusively satisfied by the sheriff's sale and return (T. R. 20); for the reasons that, as set out in the Exceptions to said Report (T. R. 22):

(1) The sale was afterwards declared void; and as a matter of law and equity, when property is sold under execution and the purchaser pays and a satisfaction is entered, but the sale proves to be invalid, the satisfaction becomes null and should be regarded as of no force and effect; there is in law no satisfaction and the judgment stands and the purchaser or his successors are subrogated to all rights of the judgment creditor against the defendant.

(2) The disallowance of this claim will result in inequity because, as stated by the Special Master (T. R. 17 and 18), the Intermountain, defendant, was paid in full for the Certificate by Margaret Cobb, and no payment whatever has ever been returned or made by it or its Receiver to Cobb or her succes-

sors including appellants who paid the sum of $1064.06, the full amount under the judgment and bid on the void sale, and who have thereby paid under the "coercive process" of the law the debt of the Receiver and will be the losers.

SPECIFICATION OF ERROR No. 2:

The Court erred in failing to render judgment for the appellants herein, approving their judgment claim filed, for the reasons stated in the above specification.

SUMMARY OF ARGUMENT

A. The Special Master found and stated the Facts in his Report. No exception was made to these Findings of Fact. The Court in its order overruling exceptions of appellants to the Conclusion of Law in the Report, made no different findings, as is required when there are disputed matters in such a Report, on the Facts. The Findings of Fact as made by the Special Master and confirmed by the Court are final and conclusive.

B. But where Findings of Fact are conclusive, the Conclusions of Law are not conclusive, and appeal can be made, as in this case, upon the ground that the Conclusions of law are not supported by the undisputed facts.

C. The finding and conclusion of the Master confirmed by the Court, that the judgment in Cobb v Intermountain Association in the State Court,

established the existence, amount and validity of the claim of appellants as against the Receiver is correct and cannot be disputed by either party.

D. But the Conclusion of Law (T. R. 20) that the sheriff's return in said Cobb case showing full payment of the amount of judgment bid on execution sale, afterwards declared void, satisfied the claim and the debt of the Receiver, is erroneous and inequitable. The Receiver has paid nothing, but the appellants advanced the money and paid Margaret Cobb. Appellants never received the property they paid for, but it was restored to the Receiver because the sale was declared void. Appellants are therefore in law and equity subrogated to the right to receive from the Receiver the debt owed. The United States Supreme Court statement in the Davis case above quoted is exactly applicable: Nothing could be more unjust than to let the debtor get his property back, and yet let his debt be discharged by the void sale.

ARGUMENT

A. The Special Master found and stated the Facts in this Report. No exception was made to these Findings of Fact. The Court in its order overruling exceptions of appellants to the Conclusion of Law in the Report, made no different findings, as is required when there are disputed matters in such a Report, on the Facts. The Findings of Fact as made by the Special Master and confirmed by the Court are final and conclusive.

The issue on this appeal is simply whether the conclusion of law and decision rejecting the claim on the ground that the satisfaction on a void sale prevents approval are supported by these findings of fact.

If the Court had considered there was any dispute of fact in the Report, specific findings thereon should have been made by the Court. The action of the Court in approving without making any specific findings is further clear proof if any were necessary that there was no disputed fact. Otherwise the case might be remanded:

O'Brien, 1937 Cumulative Supplement Manual Federal Appellate Procedure, page 20.
Wyant v. Caldwell, 67 Fed. (2nd) 374.

B. But where Findings of Fact are conclusive, the Conclusions of Law are not conclusive, and appeal can be made, as in this case, upon the ground that the Conclusions of law are not supported by the undisputed facts.

This proposition is beyond dispute, and the question for review here is whether on the undisputed facts there is an error of Law in the conclusion and decision rejecting the claim on the ground stated.

Allen v St. Louis Bank, 120 U. S. 20; 30 L. Ed. 537.
Roberts v Benjamin, 124 U. S. 64; 31 L. Ed. 336.
Edenborn v Sim (CCA 2nd) 206 Fed. 275.
D. L. & W. Co. v. Caboni, 223 Fed. 631.
White v Ball Co., 223 Fed. 619.
Aronstam v All Russian Union, 270 Fed. 460.

David Lupton Co. v Auto Club, 225 U. S.; 56 L. Ed. 1177.
American Pipe v Westchester, 292 Fed. 947.
Budd v Wilson, 7 Fed. (2d) 747.

C. The finding and conclusion of the Master confirmed by the Court, that the judgment in Cobb v. Intermountain Association in the State Court, established the existence, amount and validity of the claim of appellants as against the Receiver is correct and cannot be disputed by either party.

This proposition, and the finding and conclusion of the Special Master, and adopted by the Court (T. R. 19), that the judgment stands conclusive as it established the right to recover the amount sued for, is amply supported.

Pine Lake v. LaFayette, 53 *Fed.* 853:
This case held that a judgment, obtained even after receiver was appointed, establishes the claim.

New York Life v. Bangs, 103 *U. S.*, 26 *L Ed.* 608:
The contract is merged in the judgment and concludes all matters in relation to the contract.

Estes v. Estes, 24 *Fed.* (2d) 756:
The judgment is conclusive as to the existence and amount of the claim.

International Great Northern v. Clerk, 4 *Fed.* (2d) 19
Dillingham v. Hawk, 60 *Fed.* 495
Penn. Steel Co. v. Street Railroad, 161 *Fed.* 787
Pringle v. Woolworth, 90 *N. Y.* 510:

The judgment versus the company established as versus the receiver the amount of the debt or claim of the plaintiff.

D. But the Conclusion of Law (T. R. 20) that the sheriff's return in said Cobb case, showing full payment of the amount of judgment bid on execution sale, afterwards declared void, satisfied the claim and the debt of the Receiver, is erroneous and inequitable. The Receiver has paid nothing, but the appellants advanced the money and paid Margaret Cobb. Appellants never received the property they paid for, but it was restored to the Receiver because the sale was declared void. Appellants are therefore in law and equity subrogated to the right to receive from the Receiver the debt owed. The United States Supreme Court statement in the Davis case above quoted is exactly applicable: Nothing could be more unjust than to let the debtor get his property back, and yet let his debt be discharged by the void sale.

The conclusion, that the payment of the full sum by a third party on a void sale, satisfied the claim and the debt of Intermountain, is not supported by the facts found and is erroneous and inequitable. The Special Master (T. R. 21) recognized and reported the inequity.

The rule of law applicable is that the debt of a party whose property is sold at a void execution sale, and it is recovered by him, is not discharged. But the purchaser, or those in his place and stead, on the void sale, regardless of whether he is the judgment creditor or not, is subrogated to the right of the creditor. A purported satisfaction is, in law, no satisfaction, and judgment stands.

In the case at bar the debtor, Intermountain, through its Receiver, recovered back and retained

what was sold at the execution sale, afterwards declared void; the said debtor (Receiver) *has never paid the debt* established by the judgment, and seeks to profit by claiming *that the void sale discharged his debt* (T. R. 18 and 21). The rejection of the judgment claim if sustained would cancel the debt, and allow the Receiver to discharge the indebtedness without any payment back of money paid by Cobb to the Intermountain. In the case of *Davis v. Gaines*, 104 *U. S.* 386, 26 *L. Ed* 764, the debtor sought to have his debt discharged by a void sale. The Court confirmed the principle which should govern this case, by approval of the following:

> "Nothing could be more unjust than to permit a debtor to recover back his property because the sale is irregular, and yet allow him to profit by that irregular sale to discharge his debt."

Other courts have similarly refused to allow such an unjust result to be sanctioned:

In *Massie v. McKee*, (*Tex.*) 56 *S. W.* 119, plaintiff had bid in the full amount for land which was found not to belong to the judgment debtor. The return of the Sheriff showed satisfaction, and the plaintiff, purchaser, moved the lower court to vacate the satisfaction and this was refused. The appellate court stated that the lower court erred, that it would be inequitable to hold that the levy had the effect to satisfy the debt.

Townsend v. Smith, 20 *Tex.* 465, 70 *Am. Dec.* 400,

states the same principle. The plaintiff recovered a judgment and bid in land, which had to be given up. He then sued on the judgment, which was objected to. The appellate court stated that the sale and purchase for the full amount was not a satisfaction, if no title passed. That the judgment remains in full force. That "It does not lie with defendant to say the judgment was satisfied when by reason of nullity he recovered back the property sold." "A void proceeding cannot operate as a satisfaction of a judgment."

In *Mahrhoff v. Diffenbacher* (*Ind.*), 31 *N. E.* 41, the plaintiff purchased at the sale for the full amount and satisfaction was entered. The sale was void. The appellate court said it makes no difference whether purchaser is the judgment creditor or not, the purchaser received no value on the sale. "To deny relief . . . would be repugnant to established principles of equity and justice."

Where a sale on execution under a judgment is afterwards found void, any satisfaction entered is also void. This is the well settled rule. In *Smith v. Reed*, 52 *Cal.*, 17 *Pac. St. Rep.* 345, the full amount was bid and satisfaction entered. The execution and sale were void. The Court states that the purchaser acquired nothing by the attempted sale. That not only the execution and sale, but also the apparent satisfaction, ought to be set aside as void.

In *Copeland v. Colorado Bank* (*Colo.*), 59 *Pac.* 70

there had been a satisfaction on a sale, and the latter being void the purchaser requested vacating of the satisfaction. The appellate court states: The levy of this execution was therefore void. The subsequent proceedings depended for their validity upon the levy, and, as it was void, so were they. There was in law no levy, no sale, and no satisfaction.

In *Merquire v. O'Donnell, (Cal.)*, 72 *Pac.* 337, there was a sale and satisfaction. The sale was afterwards held void in another suit. Motion to set aside the satisfaction was denied. The appellate court said the denial should be reversed. "It is certainly necessary and consonant with the principles of equity that a party should have relief in cases where the execution and sale are void."

In *Knaak v. Brown*, 212 *N. W.* 431, 51 *A. L. R.* 241, the court states: "In fact, an entry of satisfaction is but a receipt, and like a receipt may be explained or avoided by satisfactory evidence that the payment was not in fact made, or though made satisfaction has become inoperative by reversal of judgment, vacating of sale, or any other cause rendering it inequitable for the defendant to avail himself of the entry of satisfaction.

In *Farmer and Sons v. Sasseen (Iowa)*, 18 *N. W.* 714, the court states "Where the sale has been judicially set aside . . . it necessarily follows that the satisfaction of the judgment which followed the sale,

and was entered of record by reason thereof, should be set aside."

In *Kercheval v. Lamar*, 68 *Ind.* 442, quoted in Note to 51 A. L. R., p. 258g, the court said: If the appellants got nothing by their purchase, by reason of the defective proceeding, their judgment is not satisfied in equity, and they are entitled to have the levy, sale, deed and entry of satisfaction set aside and their judgment reinvigorated and declared in full force."

The purchase money for the mortgage bought at the void sale, and paid by appellants, was received by Cobb, being full payment (T. R. 20), as creditor of the Intermountain. And appellants were subrogated to the rights Cobb had originally; that gave them the right as the judgment creditor to file claim and collect from the Receiver. The assignments (T. R. 15) of Cobb and Barrett simply were confirmatory of the subrogation allowed in law and equity. The great weight of authority including the U. S. Supreme Court in Davis v. Gaines, establishes that the purchaser or his successors at a void sale are subrogated to the rights of the judgment creditor to recover from the judgment debtor:

> A purchaser in good faith at a void execution sale is not a volunteer, and is subrogated to

the rights of creditors to the payment of whom the purchase money was applied.

60 *C. J.* 799.

Subrogation is the substitution of another person in the place of a creditor so that the person in whose favor it is exercised succeeds to the right of the creditor in relation to the debt . . . It rests upon the maxim that no one shall be enriched by another's loss, and may be invoked wherever justice demands its application, in opposition to the technical rules of law which liberate securities with the extinguishment of the original debt.

Wilson v. Todd (*Ind.*), 129 *A. L. R.* 195 *and* 196.

Purchasers at a void judicial sale are entitled to be subrogated to the rights of the creditors whose claims were discharged by the proceeds of such sale. The maxim of caveat emptor does not apply to a judicial sale where the defect in the title of a purchaser is occasioned by some irregularity in the proceedings depriving them of the power to divest the title held by the defendant.

Bond v. Montgomery (*Ark.*), 20 *S. W.* 525; 35 *Am. St. Rep.* 119.

To the same effect are:

Liverman v. Lee (*Miss.*) 38 *So.* 658, cited in 129 A. L. R. 203.

Bruce v. Spears (*Miss.*), 187 *So.* 756, cited in 129 A. L. R. 203.

Ruling Case Law also states the principle recognized and applicable to our case:

As already seen, while the right to subrogation will not arise in favor of a mere volunteer, it exists in all cases where the payment is

favored by public policy. It is upon this principle that purchasers at void judicial sales are protected, the reason in all such cases being that public policy demands that such purchasers should be encouraged by giving equitable relief to purchasers whose money has been honestly applied to the purposes to which the property has been devoted, although on account of the insufficiency of the proceedings they have failed to obtain title. It is established by the great weight of authority that where purchase money, paid over on a judicial sale that turns out to be void, is applied to the extinguishment of claims that were enforcable against the assets of an estate and for the payment of which the property might have been sold, the purchaser, if he purchased in good faith and without knowledge of the invalidity of the sale is entitled to be subrogated to the rights of the creditors whose claims were so discharged, against the property sold or its proceeds.

25 *R. C. L., p.* 1356, citing among other cases, *Davis v. Gaines*, 104 *U. S.*

Also:

The purchaser at a void execution sale is subrogated to all the rights of the execution creditor bringing about the sale. His equity rests, not upon the want of knowledge as to title in the property, but on the ground of his having discharged a judgment against the defendant, for which he stood chargeable, by a purchase, made under the coercive process of the law, and therefore he has an equitable claim to reimbursement by the defendant in execution.

25 *R. C. L., p.* 1360.

CONCLUSION

The facts found and confirmed by the Court show that the debt owed Cobb by the Intermountain (Re-

ceiver as successor) was paid in full on the execution sale. Appellants paid this money, but have received nothing, and the Receiver has paid nothing on the debt.

The cases above cited agree with the clear statement of the principle applicable, as declared by Davis v. Gaines, Supreme Court decision, which quotes with approval:

> "Nothing could be more unjust than to permit a debtor to recover back his property because the sale is irregular, and yet allow him to profit by that irregular sale to discharge his debt."

It is respectfully submitted that following this controlling case, as well as the great weight of other authority as stated in the Davis case, the order of the lower court rejecting the judgment claim should be reversed, and appellant's claim allowed as a judgment claim in the sum of $1064.06, or the case remanded with instructions to allow it, or such other order be made as this Court deems equitable to appellants.

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United States Circuit Court of Appeals

FOR THE NINTH CIRCUIT

A. H. FAVOUR and A. G. BAKER,
Appellants,

vs.

HARRY W. HILL, Receiver of Intermountain Building and Loan Association,
Appellee.

No. 9847

BRIEF OF APPELLEE

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United States
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FOR THE NINTH CIRCUIT

A. H. FAVOUR and A. G. BAKER,
Appellants,

vs.

HARRY W. HILL, Receiver of Intermountain Building and Loan Association,
Appellee.

No. 9847

ABSTRACT OF THE CASE

The Special Master found that on April 30, 1934, one Barrett paid in cash to the record attorneys of Margaret Cobb the entire amount called for in the judgment she had obtained against the Association. The Court below approved and adopted this finding and it is not challenged by the appeal. From this undisputed fact the Special Master concluded as matters of law that: (1) the cash payment was made and received in full satisfaction of the Cobb judgment; (2) that it is not necessary for an execution to issue or a judicial sale to be held in

order to work the satisfaction of a judgment, inasmuch as the test of satisfaction is whether the judgment creditor has received full payment; (3) that by reason of her receipt in cash of the entire sum called for by her judgment Margaret Cobb had no subsisting judgment rights to assign; (4) that the assignees of Margaret Cobb ocupied no better position and had acquired nothing by assignment; (5) that any right on the part of appellants to recover against the Association or the Receiver must rest on something other than the vitality of the Margaret Cobb judgment under which they claim; (6) that if Margaret Cobb could not recover as against the Association or the Receiver following her receipt of the entire amount called for in the judgment, then likewise her assignees cannot recover. The foregoing conclusions of law were adopted and approved by the Court below. The sole point raised on the appeal is that the conclusions of law are erroneous.

Our position is not limited to the narrow confines attributed to us in appellants' abstract of the case. We rely upon all of the legal conclusions drawn by the Special Master and adopted by the Court below. We further contend that even if the Cobb judgment was not extinguished by payment its ownership, for whatever it is worth, is in one Barrett. Barrett is not a party to these proceedings and is asserting no demand against the Association or its Receiver. We claim that no justiciable controversy is presented because appellants are unable to show a record ownership of the Cobb judgment. That ownership, assuming that the judgment has survived, is vested in Barrett. His rights, if any thereunder were not before the Court below and are not involved on this appeal.

SUMMARY OF ARGUMENT

I

Appellants claiming to be creditors of the receivership estate by reason of the Cobb judgment assertedly assigned to them, are unable to show privity of contract or estate with Cobb. It affirmatively appears that appellants are without privity of contract or estate and that one Barrett is the owner of the Cobb judgment. Since ownership of the Cobb judgment is the sole basis of the appellants' claim, we submit there is an absence of a justiciable controversy.

II

The conclusion of law that the payment of $1,064.06 to Margaret Cobb, which was made and received in full satisfaction of her judgment, extinguished and satisfied it so as to leave her nothing to assign, is fully and fairly supported by the undisputed facts.

A money judgment is extinguished and nothing passes by its assignment, if it appears without dispute that the judgment creditor has been fully paid in cash and that such payment was made and received with the intention of satisfying the judgment.

III

A money judgment is a non-negotiable instrument, and if assigned passes subject to all defenses available to the judgment debtor. Margaret Cobb, the judgment creditor, was paid in full and in cash prior to any assignment of her judgment. She could not file a judgment creditor's claim following her receipt of full pay-

ment, and her assignees who had notice of the facts, stand in no better position. Since the plea of payment of the judgment is good as against her, it is good as against her asserted assignees.

IV

An appellant is bound by the pleadings or the theory under which he proceeded in the trial court and on appeal he may not for the first time raise new or additional matters which were not presented below. Appellants' claim was not filed on the theory that they were subrogees. That theory was first presented on appeal. The sole basis of appellants' creditors' claim, as found by the Special Master, was that they claimed as assignees of the Cobb judgment. Hence, on appeal they cannot raise the new and additional ground that they are subrogees.

ARGUMENT

Appellants' Specifications of Error Nos. 1 and 2

A

The only question presented is whether the lower court clearly erred in affirming and adopting the Special Masters conclusion of law. Appellants' creditors' claim was filed and proceeded upon the sole theory that they were assignees of the Margaret Cobb judgment and hence occupied the status of unpaid judgment creditors (Tr. 10-11). Appellants' claim as filed with the Receiver did not purport to be based upon the doctrine of subrogation. The present assertion of appellants that

they are subrogees was not presented either to the Special Master or the court below and is mentioned for the first time on this appeal.

In their statement of facts (Op. Br. 6) appellants assert that following the sheriff's return of sale *both* Cobb and Barrett assigned their interests in the judgment to appellants. This statement is contrary to the record. On May 17, 1934, seventeen days after the sheriff's sale, Margaret Cobb, who had previously received $1,064.06 in cash in full satisfaction of her judgment, purportedly assigned it to R. O. Barrett (Tr. 15). Barrett paid $10.00 and other valuable consideration for the assignment (Tr. 15), in which Margaret Cobb expressly covenanted that the judgment was in full force and that the sum of $1,000 with interest and costs remained owing thereunder (Tr. 15). According to the record this is the first and only assignment of the judgment attempted to be made by Margaret Cobb. Thus, it is apparent that if her judgment was still subsisting and still unsatisfied notwithstanding her receipt of all the money it called for, it passed by way of assignment to Barrett and not to appellants. If appellants own the Cobb judgment and if it is still subsisting they must trace their title back to Margaret Cobb, the original owner. This we submit is physially impossible without doing violence to the record since the only assignment appellants have is the one of April 30, 1934, which they took from Barrett (Tr. 15). The time element, which appellants either overlook or disregard, shows without dispute that on April 30, 1934, Barrett was not the owner of the Cobb judgment and no assignment thereof from Margaret Cobb was outstanding. Barrett did not receive an assignment of the judgment from Margaret

Cobb until seventeen days later (Tr. 14). Hence, on April 30, 1934, Barrett had no assignable interest in the judgment and of course could assign nothing to appellants. If the Cobb judgment is still outstanding and if it still possesses vitality, all of which we dispute Barrett is the owner thereof by the assignment of May 17, 1934. Barrett has not filed a claim with the Receiver nor has he made any appearance before the Special Master or the court below. Barrett is not a party to this appeal and his rights, if any, cannot be here determined. To us it seems clear from the undisputed facts that appellants have not owned nor do they now own the Cobb judgment, be it alive or discharged. The ownership, for whatever it is worth, is in Barrett, who so far as the record discloses has never made any assignment since May 17, 1934, when Margaret Cobb, the original owner, assigned to him. No justiciable controversy is presented to this court.

B.

In no manner waiving the foregoing position, we will proceed further with appellants' argument.

On April 30, 1934, immediately prior to the sheriff's sale, Margaret Cobb had a money judgment against the Association for $1000 plus interest and costs. At the sheriff's sale Barrett, a stranger to the proceedings in which the judgment was rendered, purported to purchase a mortgage owned by the Association and judgment debtor (Tr. 11-13). For this mortgage Barrett successfully bid the whole amount of the judgment and thereupon in cash paid to the plaintiff, through Favour and Baker, her attorneys of record, the sum of $1,064.06

(Tr. 14, 20). The sale and purchase was not a paper transaction such as exists when a judgment creditor bids in property of the judgment debtor without any actual cash being manually paid. As the Special Master and the Court below found, Margaret Cobb received in cash $1,064.06, which was the entire amount due under her judgment (Tr. 14, 20). So far as the record shows, she has never repaid it. Certainly, no one would contend that after receiving every penny called for in the judgment Margaret Cobb could have compelled the Association or its Receiver to pay her any further sums. As to her the judgment was and is satisfied in full. She had no further rights against the Association, either as judgment creditor or otherwise. Absent the subsequent attempted assignment of her judgment we think it must be conceded that she could not have filed a claim with the Receiver based on the theory that her judgment was unpaid. If she could not file such a claim in her own name and right, then how can appellants, who claim to be her assignees, assert that they have greater rights? All that they could take, assuming they could trace their title back to Margaret Cobb, would be such rights as she had to assign and, as we have demonstrated, there were none in existence. See 5 *Corpus Juris,* page 963, pp. 150, wherein it is said:

> "Nothing will pass to the assignee if the assignor never had the right claimed under the assignment, or if, having had it, he had already disposed of it, *or had settled the claim on which the right was based.*" (Emphasis ours)

Our position also finds ample support in Section 21-515, *Arizona Code Annotated,* 1939, which reads:

> "An assignment of a chose in action shall not prejudice any set-off or other defense existing at the time of the notice of the assignment; but this section shall not apply to a negotiable promissory note or bill of exchange, transferred in good faith and upon good consideration before due."

If the defense of payment was available to the Association following the sheriff's sale and prior to any attempted assignment of the judgment by Margaret Cobb, then it follows under the Arizona code provision above mentioned that any assignment of the judgment was without prejudice to such existing defense, namely, the defense of payment.

Even absent a controlling statute upon the subject matter, the following rule of law would govern:

> "On a purchase and assignment of a judgment the rule of caveat emptor is generally applied in the same manner as in the purchase of any personal property. The general rule is that the assignee of a judgment stands in the place of, and has no better rights in regard to the judgment than, the assignor and that the assignee takes the judgment subject to all the equities and defenses which could be asserted against the judgment in the hands of the assignor at the time of the assignment, even if the assignee does not at the time of the assignment have notice of the outstanding equity or defense." 30 *Am. Juris.*, page 891, pp. 133)

The same rule is declared in 34 *Corpus Juris,* page 647, pp. 996.

On April 30, 1934, when Barrett attempted to assign the Cobb judgment to appellants he knew that the sum he had bid and actually paid in cash satisfied the judgment and that it possessed no further vitality. At that time he also knew he held no assignment from Margaret Cobb. He assumed that he had bought the mortgage offered at the sheriff's sale and that he was the owner thereof. Such assumption necessarily continued until November 28, 1938, when the Supreme Court of Arizona, in *Hill v. Favour, et al.*, 84 Pac. (2d) 575, 52 Ariz. 561, decided that the Association was still the owner of the mortgage. Up to that time no one thought that the Cobb judgment possessed vitality after payment on it had been made in full. Up to that time no creditor's claim had been filed on the judgment or otherwise. This same state of mind may equally be charged to appellants, who were the record attorneys for Margaret Cobb in the proceeding through which he obtained her judgment and who endorsed their satisfaction in full on the sheriff's return when Cobb bid and paid $1,064.06 in cash.

On and after April 30, 1934, Barrett and the appellants had full personal knowledge that the Cobb judgment had been paid in full and in cash and that it was satisfied of record, and that Margaret Cobb had no subsisting claim against the Association or its Receiver.

That the levy and sheriff's sale were held for naught nearly five years later, in *Hill vs. Favour, supra,* does not change the legal effect of the actual payment in full received by Margaret Cobb. She received every penny called for in her judgment, and if that payment satisfied her judgment, as we contend it did, then Sec-

tion 21-515 and the authorities we have cited must be given effect.

The satisfaction of a judgment means the payment of the money due thereunder and of course there can be but one satisfaction of judgment. 31 *Am. Juris.*, page 354, pp. 862. A judgment can be satisfied both in law and in fact without a record entry. The payment of the judgment is the satisfaction—the Clerk's entry is but evidence of the ultimate fact.

It seems to us that appellants' remedy, if they feel aggrieved, is to proceed against Barrett, who was their assignor, on the theory that there was a failure or absence of consideration for the assignment he gave them. Barrett if he were held liable on such a proceeding, could then undertake to recover from Margaret Cobb the money he paid her, inasmuch as in her assignment to him of May 17, 1934, she personally covenanted that the whole amount of the judgment with interest and costs was then unpaid. This thought finds support in 34 *Corpus Juris*, page 648, 649, pp. 998:

> "A bona fide purchaser of a judgment from an assignee takes the same subject to any equities between the judgment creditor and the assignee. The assignor is liable in damages to the assignee if the assignor does not in fact own the judgment, or if it has been extinguished wholly or partially before the assignment, or if he afterwards receives payment of the judgment or enters satisfaction of it, or if it is reversed or set aside after the assignment."

See also: *Jones v. Blumenstein* (Iowa) 42 N. W. 321.

The decision in Hill v. Favour, *supra,* and the order of the Superior Court of Yavapai County, Arizona, dated September 28, 1939 (Tr. 17) did not in any way change the position of Margaret Cobb or deprive the Association and its Receiver of the right to plead payment. Notwithstanding the decision of the Supreme Court of Arizona and the subsequent order of the Superior Court of Yavapai County, the fact remains that Margaret Cobb received every cent of money called for in her judgment and this we think every one will agree constituted full payment to her. The defense of payment, being good as against her, is good as against her claimed assignees.

As pointed out by the Special Master, appellants may have some remedy but "it must rest on something other than the vitality of the judgment of Margaret Cobb." (Tr. 21)

C.

Appellants have cited numerous authorities, both text and case, all of which in substance hold: WHERE THE JUDGMENT CREDITOR RECEIVES NOTHING OR IS NOT FULLY PAID HE OR HIS ASSIGNS MAY THEREAFTER BE RELIEVED FROM AN IMPROVIDENTLY ENTERED SATISFACTION OF THE JUDGMENT IN QUESTION. Doubtless this rule is sound and if the facts at bar were such as to warrant its application it might well be said that appellants' position is meritorious. However, the rule is not applicable because it affirmatively appears that Margaret Cobb, the judgment creditor, was actually paid cash in

hand the full amount of her judgment. This sum so far as the record shows has never been repaid or demanded back. It cannot be said that as to her there was any want or failure of consideration, or that so far as she was concerned her judgment was improvidently satisfied. Whether Margaret Cobb received the payment at a sheriff's sale subsequently declared void, or whether she received the money at home before the sale are immaterial. The time, place or circumstances of the payment are not material. The inescapable and unanswerable fact is that she did receive in cash the full amount of her judgment and that it was offered and paid to her in full satisfaction. To work a satisfaction, it is not necessary that there be a valid sale, or any sale after judgment. The test is whether or not the judgment creditor has been fully paid. The fact that Margaret Cobb has been fully paid, as found by the Special Master and the Court below, is not in dispute. Proceeding from that undisputed fact it certainly was not error for the Special Master and the Court below to conclude that the Cobb judgment could not form the basis of a valid creditor's claim.

According to the records, appellants did not predicate their claim upon the theory that they were subrogees or purchasers of the mortgage at the sheriff's sale. Their claim, as the record shows, is based solely upon the proposition that they are the *assignees* of the Margaret Cobb judgment (Tr. 11) and that by reason of the assignment they are entitled to enforce her judgment through the medium of a creditor's claim against the receivership estate. We say that since Margaret Cobb could not enforce her judgment after she had received and retained

full payment, it follows that her asserted assignees have no other or greater rights.

In the case of *Davis v. Gaines,* 104 U. S. 386, 26 L. Ed. 764, relied upon so earnestly by appellants, we find an entirely different set of facts than those at bar. All that the Supreme Court decided in the Davis case was this:

> "What we decide on this branch of the case is this: when the purchase-money paid by a purchaser in good faith, of real estate of a decedent ordered to be sold by a Probate Court, has been applied to the extinguishment of a mortgage executed by the decedent upon the property sold, and constituting a valid incumbrance thereon, and it turns out that the sale is irregular or void, the purchaser cannot be ousted of his possession upon a bill in equity filed by the heir or devisee, without a repayment or tender of the purchase-money so paid and applied."

We think even a casual reading of Davis v. Gaines, *supra,* will disclose a complete dissimilarity of facts and the enunciation of a limited doctrine which in no manner applies to the facts at bar.

Massie v. McKee (Tex.), 56 S. W. 119, cited by appellants, involved a set of facts in no manner paralleling those at bar. In the Massie case the plaintiff, who was the judgment creditor and the purchaser at the sheriff's sale, moved to vacate the satisfaction of his judgment because he had acquired no title or interest in the land ostensibly acquired at the sheriff's sale. The rights of

third parties, innocent or otherwise, were not involved. We think that Massie v. McKee, *supra,* is not in point because there the plaintiff and judgment creditor received no consideration whatsoever for his judgment and the ensuing satisfaction. In the case at bar Margaret Cobb, the plaintiff and judgment creditor, received in cash every cent called for in her judgment and as to her there was no want or failure of consideration with respect to the satisfaction of judgment.

The same reasoning and distinction applies to *Townsend v. Smith,* 20 Tex. 465, 70 Am. Decis. 400, which also was a case where the plaintiff and judgment creditor failed to receive any consideration from the sheriff's sale, at which he was the successful bidder.

Likewise, *Mahrhoff v. Diffenbacher* (Ind.), 31 N. E. 41, also relied upon by appellants, is distinguishable because the plaintiff, who was the successful bidder at the sheriff's sale, received no money or thing of value for the satisfaction of his judgment. The plaintiff and judgment creditor's situation was entirely different from that of Margaret Cobb who received full satisfaction of her judgment.

Smith v. Reed, 52 Cal. 345, also is not in point because it involved a judgment creditor who thought he was purchasing the property of a debtor. In this case cited by appellants it affirmatively appears that the judgment creditor, who was the successful bidder at the sheriff's sale, paid no money but simply used his judgment as a paper credit. Reed received nothing for the satisfaction of his judgment and hence the court set the satisfaction aside.

Copeland v. Colorado Bank (Colo.), 59 Pac. 70, cited by appellants, is not pertinent because, unlike the case at bar, the plaintiff and judgment creditor obtained absolutely nothing in satisfaction of the judgment. In other words, there was a complete failure of consideration insofar as the judgment creditor was concerned.

Knaak v. Brown (Neb.), 212 N. W. 431, 51 A. L. R. 241, is merely authority for the following proposition:

> "thus in case of absence or failure of consideration, the entry may be vacated, as here the consideration for the satisfaction was a deed believed to be good, but in fact worthless."

Certainly, the above rule should not be applied to the instant facts because as to Margaret Cobb (the judgment creditor), there was no absence or failure of consideration. Margaret Cobb received in cash the full amount of her judgment.

Merquire v. O'Donnell (Cal.) 72 Pac. 337, relied upon by appellants, turns upon a special statutory proceeding requiring a revival of the judgment for the benefit of a purchaser at a sheriff's sale, if such purchaser fails to obtain possession of the property he bought because of some irregularity in the sale. Aside from the fact that Merquire v. O'Donnell is decided upon a code provision peculiar to California, we must keep in mind the fact that appellants' claim is not based upon the fact that they are or should be declared to be the owners of the property sold at the sheriff's sale. Appellants' position, by reason of the theory of their creditor's claim, must necessarily be limited to that of asserted

assignees of the Cobb judgment. Their rights can be no greater than those of their assignor.

Farmer, et al. v. Sasseen, et al. (Iowa), 17 N. W. 714, also relied upon by appellants, turns upon a special code provision of Iowa. The case is also distinguishable because the plaintiff and judgment creditor received nothing in satisfaction of his judgment. In short, there was a complete absence and failure of consideration, neither of which can be claimed in the case at bar.

The same reasoning and distinction apply to *Kerchevel v. Lamarr,* 68 Ind. 442, also relied upon by appellants.

With the reasoning of that case and the numerous others upon which appellants pin their hope of reversal we have no quarrel. All that is declared in that line of decisions is that *if there is an absence or failure of consideration with respect to the judgment creditor, the sheriff's sale will be set aside.* The cases cited by appellants merely hold that if the judgment creditor is not actually paid, or if so far as the judgment creditor is concerned there has been a want or failure of consideration, that fact may be shown and relief may be granted to such judgment creditor.

D.

Appellants' assertion that they are subrogees is not entitled to weight for three reasons: *First,* it was not an element or partial basis of their claim as filed with the Receiver and the theory of subrogation was not presented to the Special Master nor urged to the court below (Tr. 7-9, and 21-23). It is a tardy afterthought and may not be raised or litigated here.

Tevis v. Ryan (Ariz.) 13 Ariz. 120, 108 P. 461; affirmed in 233 U. S. 273, 34 S. Ct. 481, 58 L. Ed. 957;

Mulrein v. Walsh, 26 Ariz. 152, 222 P. 1046;

Williams v. Klemovitz, 53 Ariz. 193, 87 P. (2d) 269;

Leggett v. Wardenburg, 53 Ariz. 105, 85 P. (2d) 989;

Pacific Finance Co. v. Gherna, 36 Ariz. 509, 287 P. 304.

Second, even if the doctrine of subrogation were available to appellants for argument, the fact remains that Margaret Cobb has never assigned her judgment to appellants. There is no privity of contract or chain of title to the judgment between her and appellants. The only assignment attempted to be made by Margaret Cobb was on May 17, 1934, and that purported assignment ran to Barrett, who so far as the record shows never thereafter assigned whatever rights he might be said to have acquired. The record merely shows that on April 30, 1934 (seventeen days before Margaret Cobb assigned to him), Barrett attempted to assign the judgment to appellants. This attempted assignment was a nullity because when it was made the Cobb judgment had been paid in cash and was fully satisfied, and for the further reason that on April 30, 1934, Barrett had no assignment of or interest in the judgment from Margaret Cobb. *Third,* the facts and circumstances of the full payment of the judgment (Tr. 13-14) and its concurrent satisfaction deny the right of subrogation. The doctrine is unavailable. 60 *Corpus Juris,* p. 722, pp. 30.

CONCLUSION

Upon the record and the clear, legal principles which are controlling, we submit that no reversible error on the part of the trial court has been made to appear and that hence the order should be affirmed.

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NO. 9847

United States
Circuit Court of Appeals
For the Ninth Circuit

A. H. FAVOUR and A. G. BAKER,

Appellants.

vs.

HARRY W. HILL, Receiver of Intermountain Building and Loan Association,

Appellee.

Reply Brief of Appellants

FAVOUR, BAKER & CRAWFORD,

A. G. Baker,
A. M. Crawford,
A. L. Favour.

The Bank of Arizona Building,
Prescott, Arizona

Attorneys for Appellants.

PRESCOTT COURIER

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ADDITONAL AUTHORITIES CITED

No. 9847

United States
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Reply Brief of Appellants

GENERAL STATEMENT IN REPLY

The six statements which Appellee claims in his Abstract of the Case were conclusions of law of the Master, ignore the undisputed facts that the execution sale was void, that Appellee received back the purchased property and has never paid his debt. These alleged conclusions are not supported by the

findings of fact, therefore, and any judgment rejecting the claim, based upon such conclusions, is not supported by the findings.

The Appellee's Brief diverts attention from the ground on which the claim was denied, as stated by the Master (T. R. 18) "The Receiver has refused to allow the claim on the judgment for the reason that it appears to have been satisfied by the Sheriff's sale held pursuant to the execution on the judgment of Margaret Cobb." The Master approved the rejection on this ground. The Brief raises questions which the Receiver did not raise below, as to the proper party and other matters. Appellee did not stipulate as to the Record and did not request additional portions. If he intended to attempt to question any findings and conclusions he should have included such parts, if there were any, showing different facts. But, as the Record here shows, there was no dispute or issue, in the lower court raising objection to the judicially settled point that Appellants were the proper parties to make the claim.

APPELLEE'S POINTS

I

In the last paragraph of his Abstract, in I of his Summary and in A of his Argument, Appellee for the first time contends that Barrett, and not Appellants,

was the party entitled to make this judgment claim against the Receiver.

This question of Barrett's status was decided clearly in Hill v Favour, 84 Pac. (2nd) 577, referred to in the Master's Report. The Arizona Supreme Court held "It is quite clear that Barrett disposed of all interest he may have acquired in the note and mortgage to the appellees (Favour & Baker) and that he can have no further interest in the action."

But even if that Court had not decided the ownership under the assignments which carried the debt, (5 C. J. 944, Par. 119; 34 C. J. 650, Par. 999; Brown v Scott, 25 Cal. 190, 8 Pac. St. Rep.) or by operation of law, the Record in the case at bar is clear. The lower Court found that appellants were assignees of Barrett. After the judgment in the Cobb case was corrected February 28, 1939, Margaret Cobb and R. O. Barrett (as set out in our Sworn Motion That Master Approve Judgment Claim) "thereafter again assigned to A. H. Favour and A. G. Baker the claimants herein, the judgment as corrected; and their claim was filed, based upon said judgment establishing the debt." (T. R. 8). No denial was made of these or any allegations. These were the facts upon which the Special Master clearly found that appellants were the proper claimants. He recognized and manifestly adopted the decision in Hill v Favour. He sets forth (T. R. 16) "The trial court found that the note and mortgage levied upon under the judgment in the Mar-

garet Cobb suit belonged to Favour & Baker, as the assignees of R. O. Barrett . . .", and "Thereafter, in February, 1939, A. H. Favour and A. G. Baker, as assignees of the judgment of Mrs. Margaret Cobb in Cause No. 12971 petitioned the Superior Court . . . ". He also states (T. R. 18 and 19) "The action of the Receiver rejecting the claim of Messrs. Favour & Baker as assignees of the judgment obtained by Margaret Cobb . . . is approved", and "Favour & Baker, as the assignees of Margaret Cobb have exactly the same rights that she assigned to R. O. Barrett, and that he in turn assigned to Messrs. Favour & Baker . . . " Appellee cannot now raise a question on appeal, and this is a justiciable controversy on the issue whether the satisfaction on void sale satisfies the debt of Appellee.

II

In II of his Summary and B of his Argument Appellee refers to the real issue: Does the void satisfaction satisfy the debt of and exonerate the Receiver from payment. Appellee claims caveat emptor applies and argues his version of the law applicable to a *valid* satisfied judgment. These do not apply when a sale is *void.* He has never cited any authority controverting the cases we cite stating clearly the different rule where a sale is void and the *purchaser* (whether judgment creditor or a third party) loses the property and receives nothing.

The remedy suggested, of a multiplicity of suits between various assignees, is not adequate or practical where the sale is void. If Cobb were compelled to pay back she would have no claim, for beside running of limitations, Appellee's case is based upon the insistence that she was through when she was paid (Appellee Brief, page 3, III). Objection of improper remedy was never raised in the record below. Our cited cases show the remedy pursued by appellants is the proper one when the sale is void. Caveat emptor applies only to valid sales, as clearly stated in Copeland v Colorado Bank (Opening Brief).

Appellee's argument is on law that might be applied in case of valid sales, but the equitable rule is different where a sale is void.

III.

In III of his Summary and C of his Argument Appellee argues that it makes no difference whether a sale is valid or void. He says, without citing authority, "Whether Margaret Cobb received the payment at a sheriff's sale subsequently declared void or whether she received the money at home before the sale are immaterial" and "The test is whether or not the judgment creditor has been fully paid." Our cases show clearly that this is not the rule or equitable on sales afterwards declared void. Appellee misreads our cases, when he states they refer simply to situations where a *judgment creditor* receives nothing.

They relate to recovery where the *purchaser* receives nothing because the sale is declared void. Many times the *purchaser* is the *judgment creditor*, but it is the *purchaser* who is protected whether he is judgment creditor or a third person. Public policy, to encourage such sales, requires protection of a purchaser, the more so if he is a third person. Our case of Mahrhoff v Diffenbacher shows that "it makes no difference whether the purchaser is the judgment creditor or not," and this is the fair and logical rule.

In the Davis v Gaines case, discounted by Appellee, the statement we quoted is approved by the United States Supreme Court as the broad principle, where because of irregular sale a debtor gets back his property.

IV.

In IV of his Summary and D of his Argument Appellee seeks to dispose of all reference to the equitable principles of subrogation by claiming these were not presented before. It does not matter whether we refer to the status of the Appellants as assignees or subrogees. Under the facts the principle, that the purchaser at execution sale who because of invalidity of sale does not receive the property he paid for can recover from the debtor, is the same whether there was an assignment or not. A legal subrogation is in effect an assignment by operation of law, and courts

compel assignments if not already made, and considered necessary.

Krotine v Link (Ohio) 173 N. E. at page 414:

> It is admitted . . . that had there been an assignment of this right the assignee could have recovered in his own name. Well, now, subrogation and the rights under subrogation are by assignment by operation of law. Whenever a man pays the debt of another under such circumstances that he is entitled to be subrogated to the creditor's place, he becomes an assignee in law . . . "

American Trust & Savings Bank v Turner (Ala) 80 S. at 178:

> The rule supported by the great weight of authority in America is that, when a party is entitled to subrogation, he is also entitled to have assigned to him every judgment, specialty or other security held by the creditor in respect to the debt, whether or not deemed at law to have been satisfied . . . and is entitled to be substituted in the place of the creditor as to all means and remedies which the creditor possessed to enforce payment of the debt secured from the principal debtor."

Even where there is no assignment and establishment of subrogation is sought, the facts of the case determine whether a party has the right (60 C. J. page 833) The facts in the Record in this case at bar show a clear case for subrogation (if there had been no assignment) of Appellants to the original right of Margaret Cobb to recover her debt due from the Association and Receiver. This claim, to recover the

money, was supported by the right growing out of subrogation, but as assignments had been made transferring the rights Appellants were entitled to under the principle of subrogation, there was no need to ask aid of court to get an assignment under subrogation. (In re Bruce, 158 Fed. at pages 129 and 130).

Although the facts before the Court in this case, in themselves, presented a case for the application of the right growing out of subrogation, still in addition the claim that Appellants were entitled under this right was mentioned to the Special Master in oral argument and also to the Court, which of course are not matters of record. But, it was specifically set out in paragraphs II and IV of Appellants' Petition for Rehearing (T. R. 28 and 29), renewing to the attention of the Court that Appellants "were by law subrogated to the rights of said original holder on her certificate, and judgment, as well as being assignees."

CONCLUSION

In a case of this nature, where a claim is presented to a Receiver, the claimant is subject to the attitude and requirements of the Receiver and to the manner of procedure directed by the Master in presentation of its case where the Receiver had rejected the claim. And where, as here, the requirements are diligently followed, and no objection has been made to the sufficiency or to the showing and no dispute is raised on

the facts and evidence presented by the claimant, it is, we submit, peculiarly a case where this Appellate Court in its review should give favorable consideration to all equitable rights that may be accorded to the claimants. The facts which stand out undisputed show that Appellants paid Margaret Cobb in full, relying on an execution sale afterwards declared void; the property so paid for was restored to the Receiver; Appellants have paid Margaret Cobb the debt owed her by the Receiver, and the Receiver has paid nothing on his debt.

The rejection of the claim places the Receiver in the inequitable position of profiting by the void sale to discharge his debt without any payment by him. The Supreme Court has clearly approved the principle that nothing could be more unjust than to allow a debtor to so profit.

It is respectfully urged that this Court recognize that justice and equitable principles demand that the rejection of the claim in this case be reversed and that it be allowed as a judgment claim, as prayed in the Opening Brief.

FAVOUR, BAKER & CRAWFORD

A. G. Baker,
A. M. Crawford,
A. L. Favour.

No. 9857

United States

Circuit Court of Appeals

For the Ninth Circuit.

GEORGE J. SOMERVILLE, also known as SLIM SUMMERVILLE,

Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,

Respondent.

Transcript of the Record

Upon Petition to Review a Decision of the United States Board of Tax Appeals.

PARKER PRINTING COMPANY, 545 SANSOME STREET, SAN FRANCISCO

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[Clerk's Note: When deemed likely to be of an important nature, errors or doubtful matters appearing in the original certified record are printed literally in italic; and, likewise, cancelled matter appearing in the original certified record is printed and cancelled herein accordingly. When possible, an omission from the text is indicated by printing in italic the two words between which the omission seems to occur.]

APPEARANCES

For Taxpayer:
H. K. WOOD, C. P. A.
EDWARD L. CONROY, Esq.,
DON CONROY, Esq.

For Comm'r:
E. A. TONJES, Esq.

Docket No. 98831

GEORGE J. SOMERVILLE, (Also known as Slim Summerville)

Petitioner,

v.

COMMISSIONER OF INTERNAL REVENUE,

Respondent.

DOCKET ENTRIES

1939

May 29—Petition received and filed. Taxpayer notified. (Fee paid)

" 29—Copy of petition served on General Counsel.

Jul. 26—Answer filed by General Counsel.

" 26—Request for circuit hearing in Los Angeles, Cal. filed by General Counsel.

" 31—Notice issued placing proceeding on Los Angeles calendar. Answer and request served.

1940

Mar. 6—Hearing set June 3, 1940 in Los Angeles, California.

Jun. 10—Hearing had before Mr. Black on the merits. Submitted. Stipulation of facts and appearance of Edward L. Conroy as counsel, filed at hearing. Briefs due 7/25/40—replies Aug. 9, 1940.

Jul. 11—Transcript of hearing of June 10, 1940 filed.

" 22—Notice of appearance of Don Conroy as counsel filed.

" 22—Brief filed by taxpayer.

" 24—Brief filed by General Counsel.

Aug. 8—Reply brief filed by taxpayer.

1941

Mar. 14—Opinion rendered, Black Div. 15. Decision will be entered for the respondent.

" 14—Decision entered, Div. 15, Eugene Black.

Jun. 3—Petition for review by U. S. Circuit Court of Appeals, 9th Circuit, with assignments of error filed by taxpayer.

" 3—Proof of service filed by taxpayer.

" 12—Statement of evidence filed by taxpayer.

" 12—Agreed praecipe for transcript filed with proof of service thereon.

" 12—Notice of filing praecipe with proof of service thereon. [1*]

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*Page numbering appearing at foot of page of original certified Transcript of Record.

United States Board of Tax Appeals

Docket No. 98831

GEORGE J. SOMERVILLE (Also known as Slim Summerville)

Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,

Respondent.

PETITION

The above named petitioner hereby petitions for a redetermination of the deficiency set forth by the Commissioner of Internal Revenue in his notice of deficiency IT: LA FHG-90D dated March 15, 1939, and as a basis of his proceeding alleges as follows:

1. The petitioner is an individual with residence at 719 Esplanade, Redondo Beach, California.

2. The notice of deficiency (a copy of which is attached and marked Exhibit A) was mailed to the petitioner on March 15, 1939.

3. The taxes in controversy are income taxes for the calendar years 1936 and 1937 and in the amounts of $3588.01 and $11,229.22, respectively.

4. The determination of the tax set forth in the said notice of deficiency is based upon the following errors:

(a) Including as taxable income to the petitioner that portion of his earnings which is taxable to his wife under the Community Property Law of the State of California.

5. The facts upon which the petitioner relies as the basis of this proceeding are as follows: [2]

(a) The petitioner was legally married during 1936 and until October 2, 1937, when final decree of divorce was entered, thereby ending the marital relationship between himself and Gertrude M. Somerville.

(b) The petitioner and his wife, Gertrude M. Somerville entered into an agreement whereby their real and personal property was divided between them and provision was made for the distribution of their community income received between September 1, 1936 and September 1, 1938.

(c) The petitioner is entitled, under the California Community Property Law, to file his income tax return reporting one-half of the community income while his wife reports the remaining one-half in her return.

6. Wherefore, the petitioner prays that this Board may hear the proceeding and find that the petitioner is entitled to report his income on a community basis until the date of the final decree of divorce irrespective of interpretations of agreements

which were entered into for the purpose of dividing their real and personal property.

H. K. WOOD
of Counsel for the Petitioner
EDWARD L. CONROY
of Counsel for the Petitioner
DON CONROY
of Counsel for the Petitioner
All 1680 No. Vine Street
Hollywood, California [3]

State of California,
County of Los Angeles—

George J. Somerville, being duly sworn, says that he is the petitioner named in the foregoing petition and is familiar with the statements contained therein and that the facts contained therein are true to the best of his knowledge and belief.

GEORGE J. SOMERVILLE

Sworn and subscribed to before me this 21st day of May, 1939.

[Seal] J. E. SIMPSON
Notary Public in and for the County of Los Angeles, State of California. [4]

EXHIBIT A

IT:LA FHG-90D

12th Floor,
U. S. Post Office and Court House,
Los Angeles, California.

March 15, 1939

Mr. George J. Somerville,
(also known as Slim Summerville)
719 Esplanade,
Redondo Beach, California.

Sir:

You are advised that the determination of your income tax liability for the taxable years ended December 31, 1936 and 1937 discloses a deficiency of $14,817.23 as shown in the statement attached.

In accordance with the provisions of existing internal revenue laws, notice is hereby given of the deficiency mentioned.

Within ninety days (not counting Sunday or a legal holiday in the District of Columbia as the ninetieth day) from the date of the mailing of this letter, you may file a petition with the United States Board of Tax Appeals for a redetermination of the deficiency.

Should you not desire to file a petition, you are requested to execute the enclosed form and forward it to the Internal Revenue Agent in Charge, 1200 U. S. Post Office and Court House, Los Angeles. The signing and filing of this form will expedite the

closing of your return(s) by permitting an early assessment of the deficiency, and will prevent the accumulation of interest, since the interest period terminates thirty days after filing the form, or on the date assessment is made, whichever is earlier.

Respectfully,

GUY T. HELVERING,
Commissioner,

By (Signed) GEORGE D. MARTIN
Internal Revenue Agent in Charge.

Enclosures:

Statement.
Form of waiver.
FHG-WSG [5]

STATEMENT.

IT:LA
FHG-90D

Mr. George J. Somerville,
(a. k. a. Slim Summerville)
719 Esplanade,
Redondo Beach, California.

Tax Liability for the Taxable Years Ended
December 31, 1936
and
December 31, 1937.

	Year	Tax Liability.	Tax Assessed.	Deficiency.
Income tax	1936	$ 7,262.77	$ 3,674.76	$ 3,588.01
Income tax	1937	19,428.92	8,199.70	11,229.22
Totals		$26,691.69	$11,874.46	$14,817.23

In making this determination of your income tax liability, careful consideration has been given to the report of examination dated December 6, 1938, and to your protest dated December 19, 1938.

A copy of this letter and statement has been mailed to your representative, Mr. H. K. Wood, 511 Taft Building, Los Angeles, California, in accordance with the authority contained in the power of attorney executed by you and on file with the Bureau.

ADJUSTMENT TO NET INCOME.

Taxable year ended December 31, 1936.

Net income as disclosed by return	$29,359.84
Unallowable deduction and additional income:	
Portion of your net income excluded from your return and erroneously reported by your wife	14,178.61
Net income adjusted	$43,538.45

[6]

EXPLANATION OF ADJUSTMENT.

Your net income from and after September 1, 1936 constitutes your separate income taxable to you under the provisions of Section 22(a) of the Revenue Act of 1936, by reason of the property settlement agreement entered into with your wife, effective on September 1, 1936. Your entire net income from salary for the full year in an amount of $61,440.46 was equally divided with your wife on an alleged basis of equal community interest, and $30,720.23 was reported by each in separate returns

filed; whereas the net income prior to September 1, 1936, in which your wife had a community interest, was only $33,083.23, with $16,541.62 properly reportable as taxable to her in lieu of the amount of $30,720.23 excluded from your net income and reported in the return of Mrs. George J. Somerville (Gertrude M. Somerville.) The addition to your net taxable income is, therefore, $14,178.61.

COMPUTATION OF TAX.

Taxable year ended December 31, 1936.

Net income adjusted		$43,538.45
Less: Personal exemption	$1,000.00	
Credit for dependent	400.00	1,400.00
Balance (surtax net income)		$42,138.45
Less: Earned income credit (10% of $14,000.00)		1,400.00
Net income subject to normal tax		$40,738.45
Normal tax at 4% of $40,738.45	$1,629.54	
Surtax on $42,138.45	5,633.23	
Correct income tax liability		$ 7,262.77
Income tax assessed:		
Original, account No. 203206		3,674.76
Deficiency of income tax		$ 3,588.01

[7]

ADJUSTMENT TO NET INCOME.

Taxable year ended December 31, 1937.

Net income as disclosed by return	$46,465.96
Unallowable deduction and additional income:	
Portion of your net income excluded from your return and reported by your wife in error	28,941.85
Net income adjusted	$75,407.81

EXPLANATION OF ADJUSTMENT.

Your net income during the period from January 1, 1937 to October 2, 1937 constitutes your separate income taxable to you under the provisions of Section 22(a) of the Revenue Act of 1936, by reason of the property settlement agreement entered into with your wife, Mrs. Gertrude M. Somerville, effective on September 1, 1936. The portion of your net income from salary for the period mentioned which you allocated to, and which was reported by, Gertrude M. Somerville in the separate return filed by her for the taxable year is, therefore, restored to your return and added to your taxable net income in an amount of $28,941.85. [8]

COMPUTATION OF TAX.

Taxable year ended December 31, 1937.

Net income adjusted		$75,407.81
Less: Personal exemption:		
Single exemption 11 months	$ 916.67	
Joint exemption 1 month	208.33	
Total exemption	$1,125.00	
Credit for dependent	400.00	1,525.00
Balance (surtax net income)		$73,882.81
Less: Earned income credit (10% of $14,000.00)		1,400.00
Net income subject to normal tax		$72,482.81
Normal tax at 4% on $72,482.81	$ 2,899.31	
Surtax on $73,882.81	16,529.61	

Correct income tax liability	$19,428.92
Income tax assessed:	
Original, account No. 207303	8,199.70
Deficiency of income tax	$11,229.22

[Endorsed]: U. S. B. T. A. Filed May 29, 1939.

[9]

[Title of Board and Cause.]

ANSWER

Comes now the respondent, by his attorney, J. P. Wenchel, Chief Counsel, Bureau of Internal Revenue, and for answer to the petition filed in the above entitled proceeding, admits and denies as follows:

1. Admits the allegations contained in paragraph 1 of the petition.

2. Admits the allegations contained in paragraph 2 of the petition.

3. Admits the allegations contained in paragraph 3 of the petition.

4. (a) Denies the allegations of error contained in subparagraph (a) of paragraph 4 of the petition.

5. (a) Admits the allegations contained in subparagraph (a) of paragraph 5 of the petition.

(b) Admits so much of subparagraph (b) of paragraph 5 of the petition as states that the petitioner and his wife, Gertrude M. Somerville, entered into a property agreement and denies the remainder of said subparagraph (b). [10]

(c) Denies the allegations contained in subparagraph (c) of paragraph 5 of the petition.

6. Denies that the petitioner is entitled to the relief asked for.

7. Denies generally and specifically each and every allegation contained in the petition not hereinbefore admitted, qualified, or denied.

Wherefore, it is prayed that the petition be denied and that the respondent's determination be in all respects approved.

Signed J. P. WENCHEL,
Chief Counsel,
Bureau of Internal Revenue

Of Counsel:
ALVA C. BAIRD,
FRANK T. HORNER,
E. A. TONJES,
Special Attorneys,
Bureau of Internal Revenue.

BMC/W 7/19/39

[Endorsed]: U. S. B. T. A. Filed July 26, 1939.
[11]

[Title of Board and Cause.]

Docket No. 98831. Promulgated March 14, 1941.

Income received by petitioner subsequent to September 1, 1936, the date of a property settlement agreement with his wife, the final judgment of divorce from whom was entered on October 1, 1937, is not community income and is taxable to him individually. The contention of petitioner that the

language of the property settlement agreement was not sufficient to change the character of future earnings from community property to separate property is not sustained. Van Every v. Commissioner, 108 Fed. (2d) 650, followed.

Edward L. Conroy, Esq., for the petitioner.
E. A. Tonjes, Esq., for the respondent.

OPINION.

Black: The Commissioner has determined deficiencies in income tax against petitioner of $3,588.01 for 1936 and $11,229.22 for 1937. These deficiencies result from the addition by the Commissioner to the income reported by petitioner on his income tax returns of income reported by petitioner's wife, which the Commissioner held to be the separate income of petitioner. The Commissioner, in explaining his adjustment for 1936, stated in his deficiency notice as follows:

> Your net income from and after September 1, 1936 constitutes your separate income taxable to you under the provisions of Section 22 (a) of the Revenue Act of 1936, by reason of the property settlement agreement entered into with your wife, effective on September 1, 1936. Your entire net income from salary for the full year in an amount of $61,440.46 was equally divided with your wife on an alleged basis of equal community interest, and $30,720.23 was reported by each in separate returns filed; whereas

the net income prior to September 1, 1936, in which your wife had a community interest, was only $33,083.23, with $16,541.62 properly reportable as taxable to her in lieu of the amount of $30,720.23 excluded from your net income and reported in the return of Mrs. George J. Somerville (Gertrude M. Somerville). The addition to your net taxable income, is, therefore, $14,178.61. [12]

In explanation of his determination of the deficiency for 1937, the Commissioner stated in his deficiency notice, as follows:

Your net income during the period from January 1, 1937 to October 2, 1937 constitutes your separate income taxable to you under the provisions of Section 22 (a) of the Revenue Act of 1936, by reason of the property settlement agreement entered into with your wife, Mrs. Gertrude M. Somerville, effective on September 1, 1936. The portion of your net income from salary for the period mentioned which you allocated to, and which was reported by, Gertrude M. Somerville in the separate return filed by her for the taxable year is, therefore, restored to your return and added to your taxable net income in an amount of $28,941.85.

The foregoing adjustments are contested by the petitioner in the following assignment of error:

The determination of the tax set forth in the said notice of deficiency is based upon the following errors:

(a) Including as taxable income to the petitioner that portion of his earnings which is taxable to his wife under the Community Property Law of the State of California.

The facts are stipulated and we adopt the stipulation as our findings of fact and summarize here only such facts as seem material to our decision.

The petitioner is an individual, with residence at Redondo Beach, California. For several years prior to October 2, 1937, the petitioner and Gertrude Martha Somerville were husband and wife, domiciled in the State of California. Their marriage relationship was terminated on the aforesaid date by a divorce granted to the wife by the Superior Court of California in and for Los Angeles County. Thereafter on December 8, 1937, the petitioner was married to Eleanor L. Somerville, his present wife. Sometime before their divorce the petitioner and Gertrude Martha Somerville became separated and were living separate and apart from each other on September 1, 1936. To settle certain business and domestic problems, including care, maintenance, and education of a minor child, the wife, as party of the first part, and petitioner, as party of the second part, entered into a written property settlement agreement on September 1, 1936, which, to the extent here material, provided as follows:

Whereas unhappy differences have arisen between said parties by reason whereof the parties hereto from henceforth can not live happily together, and by reason whereof they are now living separate and apart, and whereas on account of such unhappy differences the parties henceforth must live separate and apart, each from the other, and whereas in view of such facts it is the desire and intent, finally and absolutely, of said parties, by this indenture, to settle and forever adjust, and have settled and forever adjusted between themselves, all of their mutual and respective present and future property rights, both as to the properties which either may claim to be community property, and also as to the separate estate of each, * * * [13]

Whereas it is further desired and agreed on the part of the parties hereto, finally and absolutely, to settle and adjust by this indenture all of their mutual and respective rights and obligations one to the other arising out of their marriage relation, and also to determine and settle their respective rights of inheritance one from the other; and

Whereas the said parties hereto have, since the date of their marriage, acquired certain community property; and

Whereas there is a minor child of the parties hereto, and it is their further desire and intent

by this indenture to provide for the maintenance, care and custody of said minor child; and

* * * * * * *

Now Therefore, for and in consideration of the premises and mutual covenants herein expressed by and between the said parties hereto, the party of the second part agrees to pay to the party of the first part, and the party of the first part agrees to accept, a sum equal to one-half of the net income received by the second party from whatsoever source other than from income received from investments made during said period and other than income received by reason of testate or intestate succession, for a period of two years next and consecutively following upon and from the date of the execution and signing of this property settlement agreement, * * *

* * * * * * *

It is expressly understood and agreed that the above defined and described one-half of the net income of the second party agreed herein to be payable to the first party by the second party for said two year period, and the other covenants, promises, conveyances and transfers provided for in this agreement, are hereby expressly agreed to be in full and final settlement of any claim or claims of any kind or nature, other than otherwise disposed of in this property settlement agreement, which either party

> might or could otherwise make against the other party, or the separate estate of the other party, one against the other, whether in law or in equity or in probate; also as and for full satisfaction and settlement *or* any and all claim or claims of community property which either might or could make against the other, * * *

The contract made provisions for the disposition of a multitude of business and domestic problems not here material, including the settlement of interests in money on hand and individually owned and community assets. It also provided in part xii, that, after the date of its execution, income tax assessments "due, paid, or payable anywhere" upon the wife's income should be borne and paid solely by her and not by the husband. And, in part xii, provided that the income tax payments and/or penalties, if any, due or to become due upon the petitioner's income or upon community property income of both parties for any period during the existence of their marriage and prior to execution of the contract, should be borne and paid one-half by each of the parties. Concluding provisions of the contract included the following:

> XVII. It is further mutually understood and agreed that each of the parties may for themselves, independently of the other, control or do business in all matters the same as though he or she were single. [14]

XVIII. It is further understood and agreed that in making this final settlement of property rights that each of the parties hereto waives, *relinquishes and forever surrenders all claim or claims of every kind or nature which she or he has or might hereafter acquire in or against the property of the other now held or hereafter acquired,* including the rights of inheritance in case of death intestate or testate, which right each hereby expressly waives in favor of the heirs of the other. [Italics supplied.]

Petitioner's total net earnings from his personal services for the year 1936 were $61,440.46. From September 1, 1936, to and including December 31, 1936, petitioner's net earnings from his personal services were $28,357.23. One-half of said sum of $61,440.46, being petitioner's total net earnings for the year 1936, was reported on the Federal income tax return filed by petitioner and one-half thereof was reported on the Federal income tax return filed by Gertrude Martha Somerville.

Petitioner's total net earnings from his personal services for the year 1937 were $79,766.71. His net earnings from his personal services for the period commencing January 1 and ending October 1, 1937, were $57,883.70, and for the period commencing October 2 and ending December 8, 1937, were $15,-955.23. Petitioner's net earnings from his personal services for the period commencing December 8 and ending December 31, 1937, were $5,927.78. One-half of the sum of $57,883.70, being petitioner's net earn-

ings from his personal services for the period commencing January 1 and ending October 1, 1937, was reported on the Federal income tax return filed by petitioner, and one-half of the amount was reported on the Federal income tax return filed by Gertrude Martha Somerville. All of the sum of $15,955.23, being petitioner's net earnings from his personal services for the period commencing October 2, 1937, and ending December 8, 1937, was reported on the Federal income tax return filed by petitioner, and one-half of the sum of $5,927.78, being petitioner's net earnings from his personal services for the period commencing December 8 and ending December 31, 1937, was reported on the Federal income tax return filed by petitioner and one-half thereof was reported on the Federal income tax return filed by his present wife, Eleanor L. Somerville.

The petitioner relies upon section 161a of the Civil Code of California,[1] which provides that the interests of husband and wife in community property shall remain present, existing and *equal* during the marriage relation, although conceding that such

[1] 161a. *Interests in community property.* The respective interests of the husband and wife in community property during continuance of the marriage relation are present, existing and equal interests under the management and control of the husband as is provided in sections 172 and 172a of the Civil Code. This section shall be construed as defining the respective interests and rights of husband and wife in community property. [Added by Stats. 1927, p. 484.]

status of community interests may be altered by contract. The marriage relation in this case between petitioner and Gertrude M. Somerville terminated Octo- [15] ber 2, 1937, with the granting of the divorce. Under the aforesaid California statute the wife's one-half interest in petitioner's income would continue until the date of divorce, in the absence of any conveyance or agreement transferring that interest to her husband. Sherman v. Commissioner, 76 Fed. (2d) 810. The petitioner in his brief concedes that sections 158 and 159 of the California Civil Code authorize a husband and wife residing in that state to contract with each other the same as unmarried individuals and thereby release their properties, including personal earnings of either, from community property claims, citing Helvering v. Hickman, 70 Fed. (2d) 985; Van Every v. Commissioner, 108 Fed. (2d) 650; and Sparks v. Commissioner, 112 Fed. (2d) 774, as typical cases where contracts were construed to have such effect. The petitioner, however, seeks to distinguish the property settlement agreement in the instant case from the property settlement agreements construed in the cases cited and argues in brief that its terms bring the case within Sherman v. Commissioner, supra, where a contract there construed was held to have no effect upon community income; because, as pointed out by the court in its opinion, "There is nothing in the agreement which directly or indirectly deals with the subject of the future earnings of either husband or wife." We do not think what

the court said of the contract in the Sherman case applies to the contract which we have before us in the instant case. Clearly, it can not be said of the contract which we now construe that it does not deal with the community properties, including incomes of its parties, present and future. Its initial inducement clause, supra, declares the intent of the parties to be to "forever settle, and have forever settled and adjusted between themselves all of their mutual and respective *present and future property rights, both as to the properties which either may claim to be community property,* and also as to the separate estate of each." [Italics supplied.] This all-inclusive declaration of intent would seem to settle all question as to what the parties set out to do in their settlement. The provisions which follow this declaration of intent clearly show that the parties did carry it out and did dispose of and release each to the other all present and future interests which either party then owned or in the future could claim against the other, including community property interests.

The upshot of petitioner's contention on this point is that the contract did not say in so many words that the parties intended thereafter that the income of each should "belong to the spouse who earned it." Notwithstanding this contention of petitioner, we hold that the property settlement agreement in question did make the future earnings of either party to it the separate property of the spouse who earned it. In all its essential respects the contract is simi-

lar to the contract construed in Van Every v. Commissioner, supra, which the petitioner has [16] cited. In so far as the findings in that case show, as reported in 108 Fed. (2d) 650, the property settlement contract involved between husband and wife did not mention in so many words the income of either, but, as in the contract which we have in the instant case, having divided certain property and having provided, among other things, that thereafter the husband should pay to the wife $18,000 per annum (but no more than one-half of his net income and no less than $500 per month), it contained reciprocal release to the property transferred and to all claims against each other's property, present or future, and for settlement of all future demands or obligations. In that situation the court said that the contract was one which affected the future income of the parties and held that thereafter in virtue of said releases the income of the husband was his separate property taxable solely to him. We hold that the decision cited and others equally in point are against the contentions here made by the petitioner. Upon authority of it and other holdings we sustain the respondent herein.

Decision will be entered for the respondent. [17]

United States Board of Tax Appeals
Washington

Docket No. 98831

GEORGE J. SOMERVILLE (also known as Slim Summerville),

Petitioner,

v.

COMMISSIONER OF INTERNAL REVENUE,

Respondent.

DECISION

Pursuant to the determination of the Board, as set forth in its Opinion promulgated on March 14, 1941, it is Ordered and Decided: That there are deficiencies in income tax for the years 1936 and 1937 in the respective amounts of $3,588.01 and $11,229.22.

Enter:

[Seal] (Signed) EUGENE BLACK
Member.

Entered Mar 14, 1941. [18]

[Title of Board and Cause.]

PETITION FOR REVIEW BY THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE NINTH CIRCUIT.

To the Honorable, the Judges of the United States Circuit Court of Appeals for the Ninth Circuit:

I.

Jurisdiction

George J. Somerville, (also known as Slim Summerville) your Petitioner, respectfully petitions this Honorable Court to review the decision of the United States Board of Tax Appeals, entered on March 14, 1941, and finding a deficiency in income tax due from your Petitioner for the Calendar years of 1936 and 1937 in the respective amounts of $3,588.01 and $11,229.22.

Yeur Petitioner, at the time of filing this Petition, is a citizen of the United States and resides at Los Angeles, California. [19]

The returns of income tax, in respect of which the aforementioned tax liability arose, were filed by your Petitioner with the Collector of Internal Revenue for the Sixth Collection District of California, located in the City of Los Angeles, State of California, which is located within the jurisdiction of the Circuit Court of Appeals for the Ninth Judicial Circuit.

Jurisdiction of the Circuit Court of Appeals for the Ninth Circuit to review the decision of the United States Board of Tax Appeals, aforesaid, is

founded on Sections 1001-3 of the Revenue Act of 1926, as amended by Section 603 of the Revenue Act of 1928, Section 1101 of the Revenue Act of 1932 and Section 519 of the Revenue Act of 1934, and Section 1141 of the Internal Revenue Code.

II.

Nature of Controversy.

Petitioner and Gertrude Martha Somerville were husband and wife prior to 1936 and retained that status until October 2, 1937. A Property Settlement Agreement was entered into between Petitioner and his said wife on September 1, 1936, which provided, among other things, that each of the parties should receive one-half of Petitioner's net earnings for a period of two years from and after the date of said Agreement. No statement is contained in said Agreement that the subsequent earnings of Petitioner should be his sole and separate property, or that the share of his earnings to be received by each of the parties should be the sole and separate property of the one receiving it. In proceedings in the Superior Court of the State of California, in and for the County of Los Angeles, wherein Gertrude Martha Somerville was plaintiff [20] and Petitioner was defendant, an Interlocutory Judgment of Divorce was entered by said Court on September 28, 1936; that on October 2, 1937, a Final Judgment of Divorce was entered in said divorce proceedings.

Petitioner was a resident of the State of California during the entire years of 1936 and 1937.

The tax in question is based solely on income of $28,357.23 received by Petitioner from his personal services for that part of the year 1936 commencing September 1 and ending December 31, and his income of $57,883.70 received by him from his personal services for that part of the year 1937 commencing January 1 and ending October 1. One-half of the respective amounts of income was reported on the income tax returns of Petitioner and one-half thereof was reported on the income tax returns of his wife, Gertrude Martha Somerville, for the years 1936 and 1937.

The Petitioner contends that there is no provision in the Property Settlement Agreement which changes the character of his subsequent earnings from community property to separate property and his earnings, therefore, being community property until the marriage was terminated on October 2, 1937, he and his spouse had the right to file separate income tax returns, each reporting one-half of his income on a community property basis for all of the year 1936 and for that portion of the year 1937 ending October 1.

The Board of Tax Appeals held:

1. That the Petitioner is taxable on the entire amount of income received by him from his personal services for the period commencing with the date of the Property Settlement Agreement, to wit, September 1, 1936, to the date that Petitioner's marriage with [21] Gertrude Martha Somerville was dissolved, to wit, October 2, 1937.

2. That the Property Settlement Agreement changed the status of income earned by Petitioner subsequent to the date thereof from community earnings to separate earnings of Petitioner.

III.

Assignment of Errors.

In making its decisions, as aforesaid, the United States Board of Tax Appeals committed the following errors upon which your Petitioner relies as the basis of this proceeding:

1. The Board of Tax Appeals erred in holding that the income of Petitioner from his personal services for that part of the year 1936 commencing September 1 and ending December 31, and his income from his personal services for that part of the year 1937 commencing January 1 and ending October 1, was taxable entirely to Petitioner as his sole and separate property.

2. The Board of Tax Appeals erred in holding that the Property Settlement Agreement entered into by Petitioner and his then wife, Gertrude Martha Somerville, had the effect of changing the status of his subsequent earnings from community earnings to separate earnings.

Wherefore, your Petitioner prays that this Honorable Court may review the decision and order of the United States Board of Tax Appeals and reverse and set aside the same, and direct the said Board of Tax Appeals to hold and determine that the income of Petitioner for all of the year 1936

and that part of the year 1937 commencing January 1 and ending October 1 was community property of Petitioner and his then wife, Gertrude Martha Somerville, taxable one-half to each of said parties; and for the entry of further orders and direc- [22] tions as shall be deemed meet and proper in accordance with law.

EDWARD L. CONROY
DON CONROY
Attorneys for Petitioner
501 Taft Building
Los Angeles, California

State of California,
County of Los Angeles—ss.

Edward L. Conroy, being duly sworn, says:

I am one of the attorneys for the Petitioner in this proceeding. I prepared the foregoing petition and I am familiar with the contents thereof. The allegations of fact contained therein are true to the best of my knowledge, information and belief. This Petition is not filed for the purpose of delay, and I believe that the Petitioner is fully entitled to the relief sought.

EDWARD L. CONROY

Subscribed and sworn to before me this 29 day of May, 1941.

H. G. LYMAN
Notary Public in and for said County and State.

[Endorsed]: U. S. B. T. A. Filed June 3, 1941.

[23]

[Title of Board and Cause.]

To:

Commissioner of Internal Revenue,
Internal Revenue Building,
Washington, D. C.

J. P. Wenchel, Attorney for Respondent,
Chief Counsel, Bureau of Internal Revenue,
Internal Revenue Building,
Washington, D. C.

You are Hereby Notified that on the 3rd day of June, 1941, a Petition for Review by the United States Circuit Court of Appeals for the Ninth Circuit of the decision of the United States Board of Tax Appeals, heretofore rendered in the above entitled cause, was filed with the Clerk of the Board. A copy of the Petition as filed is attached hereto and served upon you.

Dated: June 2, 1941.

EDWARD L. CONROY
DON CONROY
Attorneys for Petitioner
501 Taft Building
Los Angeles, California [24]

Service of the foregoing Notice of Filing and of a copy of the Petition for Review is hereby acknowledged this 3rd day of June, 1941.

J. P. WENCHEL
Chief Counsel
Bureau of Internal Revenue
Attorney for Respondent

[Endorsed]: U. S. B. T. A. Filed June 3, 1941. [25]

[Title of Board and Cause.]

STATEMENT OF EVIDENCE

The above entitled cause came on for hearing at Los Angeles, California, before the Honorable Eugene Black, a member of the United States Board of Tax Appeals, on the 10th day of June, 1940, Edward L. Conroy, Esq., appearing on behalf of Petitioner, and E. A. Tonjes, Esq., appearing on behalf of Respondent.

Thereupon the parties, by their respective attorneys, filed with the Board a written Stipulation theretofore entered into by their counsel, and the cause was submitted upon the facts set forth in said Stipulation. By said Stipulation the parties agreed:

That Petitioner and Gertrude Martha Somerville were husband and wife for several years prior to 1936 and on September 28, 1936, an Interlocutory Judgment of Divorce was entered in the Superior Court of the State of California, in and for the County of [26] Los Angeles, in which proceedings Gertrude Martha Somerville was plaintiff and Petitioner was defendant, and a true copy of said Interlocutory Judgment of Divorce is attached to said Stipulation, marked Exhibit "A" and by such reference made a part thereof; that on October 2, 1937, a Final Judgment of Divorce was entered in said divorce proceedings between Petitioner and his said wife, Gertrude Martha Somerville, and a true copy of said Final Judgment of Divorce is attached to

said Stipulation, marked Exhibit "B" and by such reference made a part thereof; that Petitioner and his said wife entered into a Property Settlement Agreement on September 1, 1936, and a true copy of said Property Settlement Agreement is attached to said Stipulation, marked Exhibit "C" and by such reference made a part thereof; that the provisions of said Property Settlement Agreement were performed and carried out by the parties thereto in accordance with the terms thereof; that Petitioner remarried on December 8, 1937; that Petitioner was a resident of the State of California during the years 1936 and 1937; that Petitioner filed income tax returns for the years 1936 and 1937, true and exact copies of which were attached to said Stipulation, marked Exhibits "D" and "E" respectively and by such reference made a part thereof; that Petitioner's total net earnings from his personal services for the year 1936 were $61,-440.46; that from the date of the Property Settlement Agreement, namely September 1, 1936, to December 31, 1936, Petitioner's net earnings from his personal services were $28,357.23; that one-half of said sum of $61,440.46, being Petitioner's total net earnings for the year 1936, was reported on the Federal income tax return filed by Petitioner and one-half thereof [27] was reported on the Federal income tax return filed by Petitioner's then wife, Gertrude Martha Somerville; that Petitioner's total net earnings from his personal services for that part of the year 1937 commencing January 1 and

ending with the date one day prior to the date that the Final Judgment of Divorce was entered, namely October 1, 1937, was $57,883.70; that one-half of said sum was reported on the Federal Income tax return filed by Petitioner and one-half thereof was reported on the Federal income tax return filed by the said Gertrude Martha Somerville.

Thereupon counsel for Petitioner and counsel for Respondent stated that they had no further evidence to present and submitted the case on the stipulated facts to the member of the United States Board of Tax Appeals hearing the proceedings.

A true and exact copy of the written Stipulation and Exhibits contained therein are attached hereto and made a part of this Statement of Evidence.

Petitioner, George J. Somerville, (also known as Slim Summerville) tenders and presents the foregoing as his Statement of Evidence in this case and prays that the same may be approved by the United States Board of Tax Appeals and made a part of the record in this cause.

EDWARD L. CONROY,
DON CONROY,

Attorneys for Petitioner, 501 Taft Building, Los Angeles, California.

[Endorsed]: U.S.B.T.A. Filed June 12, 1941.

[28]

[Title of Board and Cause.]

STIPULATION

It is hereby stipulated by and between the parties hereto, through their respective counsel, that the following facts are deemed admitted and are hereby agreed to:

(1) That Petitioner and Gertrude Martha Somerville were husband and wife for several years prior to 1936, and on September 28, 1936, an Interlocutory Judgment of Divorce was entered in the Superior Court of the State of California, in and for the County of Los Angeles, in which proceedings the said Gertrude Martha Somerville was plaintiff and Petitioner George J. Somerville was defendant. A true and exact copy of said Interlocutory Judgment of Divorce is attached hereto, marked Exhibit "A" and by such reference made a part hereof.

(2) That on October 2, 1937, a Final Judgment of Divorce was entered in said divorce proceedings between Petitioner and his said wife. A true and exact copy of said Final [29] Judgment of Divorce is attached hereto, marked Exhibit "B" and by such reference made a part hereof.

(3) That Petitioner and the said Gertrude Martha Somerville entered into a Property Settlement Agreement on the 1st day of September, 1936. A true and exact copy of said Property Settlement Agreement is attached hereto, marked Exhibit "C" and by such reference made a part hereof; that the

provisions of said Property Settlement Agreement were performed and carried out by the parties thereto in accordance with the terms thereof.

(4) That Petitioner married Eleanor L. Somerville on December 8, 1937.

(5) That during the entire years of 1936 and 1937 Petitioner was a resident of the State of California.

(6) That Petitioner filed Federal income tax returns for the years 1936 and 1937, true and exact copies of which are attached hereto, marked Exhibits "D" and "E" respectively and by such reference made a part hereof.

(7) That Petitioner's total net earnings from his personal services for the year 1936 were $61,440.46; that from September 1, 1936, to and including December 31, 1936, Petitioner's net earnings from his personal services were $28,357.23; that one-half of said sum of $61,440.46, being Petitioner's total net earnings for the year 1936, was reported on the Federal income tax return filed by Petitioner and one-half thereof was reported on the Federal income tax return filed by the said Gertrude Martha Somerville.[30]

(8) That Petitioner's total net earnings from his personal services for the year 1937 were $79,766.71; that Petitioner's net earnings from his personal services for the period commencing January 1, 1937, and ending October 1, 1937, were $57,883.70; that Petitioner's net earnings from his personal services for the period commencing October

2, 1937, and ending December 8, 1937, were $15,-955.23; that Petitioner's net earnings from his personal services for the period commencing December 8, 1937, and ending December 31, 1937, were $5,-927.78; that one-half of said sum of $57,883.70, being Petitioner's net earnings from his personal services for the period commencing January 1, 1937, and ending October 1, 1937, was reported on the Federal income tax return filed by Petitioner, and one-half of said amount was reported on the Federal income tax return filed by the said Gertrude Martha Somerville; that all of the said sum of $15,955.23, being Petitioner's net earnings from his personal services for the period commencing October 2, 1937, and ending December 8, 1937, was reported on the Federal income tax return filed by Petitioner; that one-half of the said sum of $5,-927.78, being Petitioner's net earnings from his personal services for the period commencing December 8, 1937, and ending December 31, 1937, was reported on the Federal income tax return filed by Petitioner and one-half thereof was reported on the Federal income tax return filed by his wife, Eleanor L. Somerville.

Dated this 3rd day of June, 1940.

EDWARD L. CONROY,
Counsel for Petitioner.

J. P. WENCHEL,
Counsel for Respondent.

[31]

EXHIBIT "A"

In the Superior Court of the State of California
in and for the County of Los Angeles

No. D147-635

GERTRUDE MARTHA SOMERVILLE,
Plaintiff,

vs.

GEORGE J. SOMERVILLE,
Defendant.

INTERLOCUTORY JUDGMENT
OF DIVORCE

(Default)

This cause came on to be heard the 28th day of September, 1936, in Department 32, Arthur C. Miller appearing as attorney for plaintiff, and it appearing that defendant was duly served with process and has not appeared or answered the complaint, and that the default of defendant has been entered:

It is adjudged that plaintiff is entitled to a divorce from defendant; that when one year shall have expired after the entry of this interlocutory judgment a final judgment dissolving the marriage between plaintiff and defendant be entered, and at that time the Court shall grant such other and further relief as may be necessary to complete disposition of this action.

Custody of the minor child of these parties, towit: Elliott, is hereby granted to the first party, sub-

ject to the right which is hereby granted to the second party to have custody of the said child during vacation periods for a total maximum term of three months in each year, consecutively or at such vacation periods as the second party may elect, and if he so elects in whole or in part, but not including Christmas week; each [32] party is to have rights of reasonable visitation of and with the said child during the term it is in the custody of the other; each party is to have alternate week ends visitation periods and custody of the child during such time as the child is in the custody of the other party. Neither party is to take the child out of the territorial limits of Southern California without the written permission of the other party.

Each party is to provide proper and fitting home conditions for said child during all of said custody periods.

It is hereby ordered that first party is to pay the sum of one hundred ($100.00) dollars per month as and for the support and maintenance and education of said child, until further order of the Court.

Done in open Court this 28th day of September, 1936.

CHARLES L. BOGUE,
Judge.

Entered Sept. 28, 1936.

Docketed Sept. 28, 1936.

Book 949, Page 249.

NOTICE—CAUTION

This is not a judgment of divorce. The parties are still husband and wife, and will be such until a final judgment of divorce is entered after one year from the entry of this interlocutory judgment. The final judgment will not be entered unless requested by one of the parties. [33]

EXHIBIT "B"

In the Superior Court of the State of California in and for the County of Los Angeles

No. D 147-635

GERTRUDE MARTHA SOMERVILLE,

Plaintiff,

vs.

GEORGE J. SOMERVILLE,

Defendant.

FINAL JUDGMENT OF DIVORCE

In this cause an interlocutory judgment was entered on the 28th day of September, 1940, adjudging that plaintiff was entitled to a divorce from defendant, and more than one year having elapsed, and no appeal having been taken from said judgment, and no motion for a new trial having been granted and the action not having been dismissed;

Now, upon the court's own motion, it is adjudged that plaintiff be and is granted a final judgment of divorce from defendant, and that the bonds of

matrimony between plaintiff and defendant be, and the same are, dissolved.

It is further ordered and decreed that wherein said interlocutory decree makes any provision for alimony or the custody and support of children, said provision be and the same is hereby made binding on the parties affected thereby the same as if herein set forth in full, and that wherein said interlocutory decree relates to the property of the parties hereto, said property be and the same is hereby assigned in accordance [34] with the terms thereof to the parties therein declared to be entitled thereto.

Done in open Court this 2nd day of October, 1937.

INGALL W. BULL,
Judge.

This Decree Is Not Effective Until Entered in Judgment Book by Clerk

Entered Oct. 2, 1937.

Docketed Oct. 2, 1937.

Book 981, Page 240.

[Endorsed]: Filed at request of Robert G. Wheeler, 715 So. Hope St., Los Angeles, Calif., Attorney for: Defendant. [35]

EXHIBIT "C"

Property Settlement Agreement.

This agreement, made and entered into this 1st day of September, 1936, at Los Angeles, California, by and between Gertrude Somerville, wife, hereinafter known as the party of the first part or as the first party, and Geo. J. Somerville, husband, hereinafter known as the party of the second part or as the second party, both residing in Los Angeles County, State of California,

Witnesseth,

That whereas the parties hereto are lawfully intermarried, having been married at San Luis Obispo, California (G.M.S. L.F.M. G.J.S. H.F.N.) on the 19th day of November, 1927, and ever since said time having been and now being husband and wife; and

Whereas unhappy differences have arisen between said parties by reason whereof the parties hereto from henceforth can not live happily together, and by reason whereof they are now living separate and apart, and whereas on account of such unhappy differences the parties henceforth must live separate and apart, each from the other, and whereas in view of such facts it is the desire and intent, finally and absolutely, of said parties, by this indenture, to settle and forever adjust, and have setttled and forever adjusted between themselves, all of their mutual and respective present and future property rights, both as to the properties which either may claim to be community prop-

erty, and also as to the separate estate of each, and it is their desire and intent to settle and adjust, finally and absolutely, by this indenture, any and all claim or claims for alimony, separate maintenance, counsel or attorney's fees, or costs of Court in any action that may be brought for a divorce, or any action that may now be pending, between said parties, or in any action at law or other litigation, or otherwise, which either of the parties hereto may or might hereafter make one against the other; and

Whereas it is further desired and agreed on the part of the [36] parties hereto, finally and absolutely, to settle and adjust by this indenture all of their mutual and respective rights and obligations one to the other arising out of their marriage relation, and also to determine and settle their respective rights of inheritance one from the other; and

Whereas the said parties hereto have, since the date of their marriage, acquired certain community property; and

Whereas there is a minor child of the parties hereto, and it is their further desire and intent by this indenture to provide for the maintenance, care and custody of said minor child; and

Whereas the second party hereby represents that the entire community property of the parties hereto that is in his possession or control, or held for the benefit of the second party by any person, corporation or partnership other than the first party,

is fully disclosed in the following inventory, to-wit:—(G.M.S. L.F.M. G.J.S. H.F.N.)

Cash in the amount of Twenty-four thousand Fifty and 54/100 ($24,050.54), other than and in addition to Two Hundred Dollars ($200.00) upon his person which Two Hundred Dollars upon his person is elsewhere herein disposed of to be his separate property, the real properties disposed of between the parties elsewhere in this agreement, the personal properties disposed of between the parties elsewhere in this agreement, two automobiles registered in the name of the second party and being a Lincoln Automobile and a Ford V-8 Automobile disposed of between the parties elsewhere in this agreement, and personal wearing apparel, Personal jewelry, personal ornaments, radios, personal furniture or personal effects, all of which are disposed of elsewhere in this agreement; and

Whereas the first party hereby represents that the entire community property of the parties hereto that is in her possession or control or held for the benefit of the first party, or for the benefit of the minor child of the parties, Elliott, by any person, corporation or partnership other than the second party, is fully [37] disclosed in the following inventory;

The real properties disposed of between the parties elsewhere in this agreement.

The personal properties disposed of between the parties elsewhere in this agreement.

One automobile, registered in the name of the

first party and being a Plymouth coupe, disposed of between the parties elsewhere in this agreement.

Wearing apparel, personal jewelry, personal ornaments, radios, personal furniture or personal effects, all of which are disposed of elsewhere in this agreement. (G.M.S. L.F.M. G.J.S. H.F.N.) [38]

Now therefore, for and in consideration of the premises and mutual covenants herein expressed by and between the said parties hereto, the party of the second part agrees to pay to the party of the first part, and the party of the first part agrees to accept, a sum equal to one-half of the net income received by the second party from whatsoever source other than from income received from investments made during said period and other than income received by reason of testate or intestate succession, for a period of two years next and consecutively following upon and from the date of the execution and signing of this property settlement agreement, it being hereby mutually understood and agreed that for such purposes the term "net income" in this instance and wherever used in this connection in this agreement is to be defined and arrived at by deducting from the gross income of the second party received from the sources indicated above during said period of two years, each and all of the following items to-wit:—

a. Agent's and/or agents' commission and/or commissions paid or payable by the second party during the said period of two years, or payable thereafter, upon some and/or all of the gross income and/or net income of the second party during

said two years from the date of the execution of this agreement, said commission and/or commissions not to exceed ten per centum (10%) of said gross income and/or net income; and

b. Income tax assessments and/or payments assessed, due, paid or payable anywhere upon the gross income and/or upon the net income, as the case and/or cases may be, of the second party during said period of two years from the date of the execution and signing of this agreement, whether due or payable during or after said period of two years from the date of the execution and signing of this agreement; with the proviso that it is mutually understood and agreed that for the fiscal year of January 1st 1936 to December 31st 1936 that portion of the above specified income tax payments and/or [39] assessments shall be so deductible as the total number of days remaining in said fiscal year from the date of the execution and signing of this agreement bears to the total number of days in said fiscal year, without respect to the proportionate relationship that the income received by the second party from the date of the execution and signing of this agreement to the end of said fiscal year bears to the income received by the second party from the beginning to the end of said fiscal year; and with the further proviso that it is hereby mutually understood and agreed that for the fiscal year of January 1st 1938 to December 31st 1938 in which the specified period of two years provided for in this agreement shall terminate, that portion

of the above specified income tax payments and/or assessments shall be so deductible as the total number of days elapsed in said fiscal year until the date of the expiration of the two year period provided for in this agreement bears to the total number of days in said fiscal year without respect to the proportionate relationship that the income received by the second party from the first day of said fiscal year to the date of the expiration of this agreement in said fiscal year bears to the income received by the second party from the beginning to the end of said fiscal year; and with the further proviso that it is hereby mutually understood and agreed that the second party shall withhold upon receipt and out of all the above described income of the second party during the specified two year period of this agreement a percentage of the amount of said earnings and income of the second party, above described, after first deducting therefrom agent's and/or agents' commission and/or commissions, said percentage or amount withheld to be sufficient to anticipate the amount of said income tax payments and/or assessments above described in the judgment, supplied at least quarterly, of the firm of Boyle and Wood, Income Tax Counsellors, Taft Bldg. Hollywood, California, and said deducted percentage to be held by the second party for the purpose of payment of the above specified [40] income tax payments and/or assessments; and with the further proviso that it is hereby mutually understood and agreed that the second party shall pay

to the first party one-half of any balance of said percentage of his above described income for the specified two year period of this agreement remaining after payment in full out of or ascertainment and deduction of the amount payable out of the same of the herein specified income tax payments and/or assessments, such adjustment to be made within two weeks after the final dates permitted by law to file said income tax returns for the fiscal years 1936, 1937, and 1938; and with the further proviso that it is hereby mutually understood and agreed that in the event and/or events that the total of the above specified percentage of the above described income of the second party for the two year period of this agreement in any instance and/or instances shall not be sufficient to pay the above specified income tax payments and/or assessments the party of the first party shall share and pay one-half and the party of the second part shall share and pay one-half of the excess of the above specified income tax payments over and above said percentage of the above described income of the second party; and with the further proviso that it is mutually understood and agreed that both parties shall cooperate to the interest of themselves and each other in arranging for any legitimate saving upon the above specified income tax payments and/or assessments during all or any portion of the two year period of this agreement, or thereafter; and

c. It is expressly understood that the second party makes the claim that the second party is

obligated to an expenditure of at least One Hundred and Twenty-five Dollars ($125.00) weekly during those weeks when he is engaged in his occupation as an actor, or motion picture director or stage director, or other occupation or connection or employment with the motion picture industry or legitimate stage or vaudeville or other forms of entertainment [41] industry, as and for good will expenses which in their nature do not permit of a receipt for or proof of the giving and expenditure thereof being received by the second party, which weekly amount includes items of professional expenses in an amount of from approximately One Thousand Dollars ($1,000.00) to One Thousand Five Hundred Dollars ($1,500.00) per year deductible on the income tax returns of the second party for wardrobe, advertising, makeup, dues, etc., and that the second party has requested the first party to allow a further deduction from the gross income of the second party for the purposes herein of Sixty Dollars ($60.00) per week as the share of the first party and of Sixty-five Dollars ($65.00) per week as the share of the second party in said good will burden and professional expenses, so that the first party will thereby join with the second party in assuming said good will burden and professional expenses, which the first party refuses so to do to that extent; so it is therefore hereby mutually understood and agreed that the proposed share of Sixty Dollars ($60.00) per week of the first party in said good will burden and professional expenses

shall not be deducted from the gross income of the second party for the purposes herein; and it is further understood and agreed that the sum of Sixty-Five Dollars ($65.00) per week is determined and agreed by both parties hereby to be the share of the first and second parties in said good will burden and professional expenses and that the sum of Sixty-Five Dollars ($65.00) per week while the second party is working at said professions and occupations enumerated above shall be deducted from his weekly income while so working to determine, with the other deductions provided for herein, the net income of the second party for the purposes herein; and it is further understood and agreed that because of the nature of this good will burden and professional expenses as more specifically described above and otherwise and the impossibility of obtaining receipts and evidence of payments of all and/or some of it, that this deduction of Sixty-Five Dollars [42] ($65.00 per week as specified herein shall be made without any obligation upon the part of the second party to account for the expenditure of said amount.

It is expressly understood and agreed that the above defined and described one-half of the net income of the second party agreed herein to be payable to the first party by the second party for said two year period, and the other covenants, promises, conveyances and transfers provided for in this agreement, are hereby expressly agreed to be in full and final settlement of any claim or claims

of any kind or nature, other than otherwise disposed of in this property settlement agreement, which either party might or could otherwise make against the other party, or the separate estate of the other party, one against the other, whether in law or in equity or in probate; also as and for full satisfaction and settlement or any and all claim or claims of community property which either might or could make against the other, and also as and for a full and final settlement for separate maintenance of either party hereto, and a full and final settlement of any claim or claims which either might or could otherwise make for alimony, counsel or attorney's fees, or costs, or otherwise in any action for divorce now pending or that may be brought by either party hereto, or litigation which may hereafter arise between said parties, and is a full and final settlement of any and all future claim and/or claims that the first party or the second party might otherwise assert or make, one against the other, of whatsoever kind or nature, whether in law and/or in equity and/or in probate.

II.

That the second party represents that he owns and carries two life insurance policies upon the life of the second party, one being a policy in the Prudential Insurance Company, so-called, in the amount of Fifteen Thousand Dollars ($15,000.00), and the other being a policy in the Missouri State Life Insurance Company, or its [43] successor,

in the amount of Ten Thousand Dollars ($10,000.-00); with respect to these two policies it is mutually understood and agreed that the second party, during the two year period provided for in this agreement from the date of the execution and signing thereof, will not take advantage of any right or privilege reserved by the second party under the terms of either insurance policy to change the beneficiary, so-called, from the name of the first party, whom the second party represents is the present beneficiary, in each policy; and the second party further agrees and undertakes to pay all premiums on both policies until the end of the two year period from the date of the execution and signing of this agreement; it is further understood and agreed that the said policies shall be placed in escrow with the Title Insurance and Trust Company, Los Angeles, California, under written instructions to said escrow holder, signed by both parties hereto, and which signatures shall be acknowledged before a notary public and/or notaries public, instructing that the said policies shall be delivered to the first party within a reasonable time after the death of the second party, provided that such death occur within, but not beyond, the two year period from the date of the execution and signing of this agreement, and further instructing that upon the second party being alive after the expiration of the two year period from the date of the execution and signing of this agreement the said policies shall be delivered to the second party, or to the legally entitled representa-

tive of the second party, in the event as to the latter instance of the death of the second party after the expiration of the said two year period and before the said policies are delivered to the second party; and it is further understood and agreed that the first party hereby waives and releases any and all claim and/or claims the first party may have and/or assert to have of right and/or title and/or interest in and to said policies and/or the proceeds thereof and/or the value thereof and/or as beneficiary thereof, either in law or in equity [44] or in probate, and irrespective of whether or not the first party as beneficiary thereof be changed and/or not changed and/or changeable and/or not changeable in either and/or both and/or each of said policies after the expiration of two years from the date of the execution and signing of this property settlement agreement, and hereby irrevocably authorizes the change of the beneficiary of each and/or either and/or both of said policies after the expiration of said two years, without limiting the waiver and release of the first party of any and all claim and/or claims the first party may have and/or assert to have of right and/or title and/or interest in and to said policies and/or the proceeds thereof and/or the value thereof and/or as beneficiary thereof, either in law or in equity or in probate, said waiver being made irrespective of whether or not the first party as beneficiary thereof be changed and/or not changed and/or changeable and/or not changeable in either and/or both and/or each of

said policies after the expiration of two years from the date of the execution and signing of this agreement; and it is further understood and agreed that no payments shall be due and payable under this property settlement agreement until the first party shall have delivered to the said escrow holder the original of the Fifteen Thousand Policy of insurance upon the life of the second party herein referred to and shall have signed the herein provided for escrow instructions and acknowledged said signature before a Notary Public; and it is further understood and agreed that in the event the second party shall decide to let either or both of said policies lapse, after the expiration of the period of two years of this agreement, the first party shall have the option of paying the premiums thereon after a change of the beneficiary to Elliott, the minor child of the parties, and after written notice to the first party of such intention to let such policies lapse, executed, signed and acknowledged before a Notary Public by the second party, the second party agreeing to make such change or changes of beneficiary or beneficia- [45] ries after the giving by the second party of such above prescribed notice.

III.

It being represented by the second party that in his profession it is necessary for him to have a reasonable amount of cash on hand and the reasonableness of this representation being accepted by the first party, it is hereby mutually understood and

agreed that of an amount of Twenty-four thousand Fifty and 54/100 ($24,050.54) (G.M.S. L.F.M. G.J.S. H.F.N.) cash on hand and/or in the possession of and/or on deposit to the credit of the second party, which amount the second party hereby represents to be all of the cash he has on hand or in his possession or on deposit to the credit of the second party or anyone else, save and except and not including herein an amount of cash on his person not in excess of Two Hundred Dollars ($200.00), as to which amount of not in excess of Two Hundred Dollars ($200.00) on the person of the second party the first party hereby waives all her separate property and/or community property rights therein, the shall be disposed of as follows as to all community property rights and/or separate property rights and/or other property rights of the parties hereto in said cash:

1. At the expiration of two years from the date of the execution and signing of this agreement the amount of one-half of the amount of said cash remaining after payment first out of said cash during or after said two year period of the following items, shall be payable to the party of the first part by the party of the second part as her community property and/or separate property share and/or other property right and/or share of the original amount of said cash:

a. The sum of Four Thousand Dollars ($4,000.-00) of said cash shall be the sole and separate property of the second party and the first party

hereby releases and waives the same to the second party, waiving and releasing any and all claim and/or claims thereto, [46] both as to any community property and/or separate property and/or other property right therein; and

b. An attorney's fee to counsel for the second party, to-wit:—Robert G. Wheeler, Wright & Callender Bldg., Los Angeles, California, in the amount of Four Thousand Dollars ($4,000.00), for legal services rendered by said attorney to the second party and/or to be rendered to the second party in connection with the rights and claims of the second party against the first party, in or out of court, and in connection with the resistance of the rights and claims of the first party against the second party, in or out of court, and/or for the trial of any action instituted by either party against the other prior to or after the execution and signing of this property settlement agreement; and

c. An investigation fee to investigators for the second party, to-wit:—the firm of Atherton and Dunn, Rowan Bldg., Los Angeles, California, in the amount of Two Thousand Five Hundred Dollars ($2,500.00) for investigation services and other services rendered by said firm to the second party in connection with the rights and claims of the second party against the first party, in or out of court, and in connection with the resistance of the rights and claims of the first party against the second party, in or out of court, and/or for services at the trial of any action instituted by either

party against the other party prior to or after the execution and signing of this agreement; and

d. That portion of income tax payments upon the gross income and/or net income of the second party for the fiscal year of January 1st 1936 to December 31st 1936 as the total number of days elapsed before the execution and signing of this agreement bears to the total number of days remaining in said fiscal year, without respect to the proportionate relationship that the income received by the second party from the beginning of said fiscal year to the date of the execution and signing of this agreement bears to the income received by the second party from the beginning to the end of said fiscal year; and [47]

e. All income tax payments upon the joint and/or community property income tax returns of the parties hereto for the fiscal year of January 1st 1935 to December 31st 1935 not yet paid and remaining unpaid at the date of the execution and signing of this agreement; the second party in this connection representing that he has paid all income tax assessments assessed and payable by and against himself or the parties hereto jointly from the date of their said marriage until and including the second quarterly payment on their Federal income tax return and the second of a total of three payments on their California income tax return, said income tax returns being for the fiscal year of January 1st 1935 to December 31st 1935.

f. Any income tax payments and/or assessments upon the community property income of the first and second parties during the period of the married life of the parties hereto for previous fiscal years not previously covered herein and as to which there may be any further tax due or any penalties incurred; with the proviso that the parties shall each enjoy and share alike in any refund made of payments of income tax for previous fiscal years of the married life of the parties.

IV.

It is hereby mutually understood and agreed that the custody of the minor child of these parties, to-wit:—Elliott, is hereby granted to the first party by agreement, provision for custody by the first party as aforesaid to be based upon the first party providing property and fitting home conditions for said child, and maintenance of said child by the second party in the manner herein provided for, and subject to the right which is hereby granted to the second party to have custody of said child during vacation periods for a total maximum term of three months in each year, consecutively or at such vacation periods as the second party may elect, and if he so elects in whole or in part, but not including [48] Christmas Week, during which Christmas Week the first party shall continue to have custody of said child, this provision for custody by the second party by the second party for such vacations periods as aforesaid to be based upon

the second party providing maintenance and support during said custody and proper and fitting home conditions for said child during said custody periods; each party is to have rights of reasonable visitation of and with the said child during the term it is in the custody of the other; each party is to have alternate week end visitation periods and custody of the child during such times as the child is in the custody of the other party, and such other visitation periods and custody of and with said child as are mutually agreed upon by the parties; with the proviso that each party agrees to not take the child out of the territorial limits of Southern California without the written permission of the other party and shall not have the right to take the child out of the territorial limits of Southern California without written permission of the other party.

V.

The second party agrees to pay and the first party agrees to accept the sum of One Hundred Dollars ($100.00) per month as and for the support and maintenance and education of the minor child of the parties, until such time as his age and the reasonable requirements for his support and maintenance and education may require an increase; with the proviso that it is mutually understood and agreed that upon such an increase being required and allowed as expressed above the first party will every three months furnish to the sec-

ond party a written and reasonable accounting of the expenditure of said amounts.

VI.

It is mutually understood and agreed that certain property situated at 10303 Valley Spring Lane, North Hollywood, California, and more particularly described as:— [49]

> Lot 30, Tract 9354, as per map recorded in Book 126, Pages 27 and 28 of Maps in the office of the Recorder of Los Angeles County, California, (G.M.S. L.F.M. G.J.S. H.F.N.)

together with the complete and usual furniture contained on and in said property, are to and shall belong to the first party, and the second party hereby agrees to release, remise and quit-claim to the first party all right, title and interest therein whatsoever which he may have derived or claim to have derived from any source or in any manner through any provision of law or by agreement or otherwise.

VII.

It is hereby mutually understood and agreed that certain property situated on Valley Spring Lane, North Hollywood, California, and sometimes referred to as the "Mac Cray Acre, and more specifically described as follows:

As set out on Page 15 (a) hereof, (G.M.S. L.F.M. G.J.S. H.F.N.)

is to and shall belong to the first party and that the second party hereby agrees to release, remise

and quit-claim to the first party all right, title and interest therein, whatsoever, which he may have derived or claim to have derived from any source or in any manner through any provision of law or by agreement or otherwise.

VIII.

It is hereby mutually understood and agreed that certain premises and property located at 619 Sleepy Hollow Lane, Laguna Beach, California, and more particularly described as: (G.M.S. L.F.M. G.J.S. H.F.N.)

Lots Sixteen (16) and Twenty-two (22) of Laguna Beach, in the City of Laguna Beach, County of Orange, State of California, as per map thereof recorded in Book 16, at page 43, of Miscellaneous Records of Los Angeles County, California, and also all land lying between the Southwesterly line of said Lot 22 and the line of ordinary high tide of the Pacific Ocean.

[50]

That portion of Lot 217 of the Property of the Lankershim Ranch Land and Water Company, in the City of Los Angeles, County of Los Angeles, State of California, as shown on map recorded in Book 31, Page 39 et seq., Miscellaneous Records of said County, described as follows:

Beginning at a point on the Southerly line of the said Lot, distant North 88° 45′ 20″ East 12.50 feet from the Southeasterly corner of

Tract No. 9354, as shown on map recorded in Book 126 Page 28, of Maps, in the office of the County Recorder of said County; thence parallel with the Easterly line of said Tract No. 9354, North 1° 21′ 12″ West 220.00 feet; thence parallel with the said Southerly line, North 88° 45′ 20″ East 225.00 feet; thence parallel with the Easterly line, South 1° 21′ 12″ East 220.00 feet to the said Southerly line; thence South 88° 45′ 20″ West 225 feet to the point of beginning. (G.M.S. L.F.M. G.J.S. H.F.N.) [51]

together with the complete and usual furniture and fixtures contained on or in said property and all furniture therein, are to and shall belong to the second party and that the first party hereby agrees to execute and deliver to the second party a bill of sale of said furniture and a good and sufficient deed of and to said property by the first party to the second party whereby a full and complete and fee-simple title to the said property will vest immediately in the second party, free and clear of all liens, mortgages, trust deeds, taxes, assessments, or other encumbrances, easements, restrictions, or cloud upon the title granted, other than and excepting only:

1. Taxes for the fiscal year 1936-37, a lien.

2. An easement and right of way over the Northeasterly rectangular 20 feet of said Lot 16 for Coast Boulevard, as conveyed to the County

of Orange by Deed dated January 30th, 1924, and recorded in Book 512, at page 18 of Deeds, in the office of the County Recorder of said Orange County.

3. An easement and the right to construct footings for a concrete retaining wall incidental to the construction of Coast Boulevard over and across the Southwesterly 4 feet of the Northeasterly 24 feet of said Lot 16, as granted to the County of Orange by deed dated September 23, 1926, and recorded in Book 678, at page 373, of Official Records, in the office of the County Recorder of said Orange County.

4. An easement for use as a public way, street and highway over a strip of land 20 feet wide including the Southwesterly portion of said Los 16 and the Northeasterly portion of said Lot 22 as condemned to the use of the City of Laguna Beach and to the public by a judgment rendered February 5, 1931, in the Superior Court of the State of California, in and for the County of Orange in action No. 25684, a certified copy of which judgment was recorded in Book 455, at page 285, of Official Records in the office of the County Recorder of said Orange County.

(G.M.S. L.F.M. G.J.S. H.F.N.) [52]

and to further deliver to the second party a certificate of title issued by the Title Insurance and Trust Company, Los Angeles, California, showing and in-

suring that the full and complete and fee simple title to said property vests in the second party, free and clear of all liens, mortgages, trust deeds, taxes, assessments, or other encumbrances, easements, restrictions, or cloud upon the title granted, other than and excepting only those matters excepted in this connection above at page 16, after line 11, hereof; the expenses of the issuance of said certificate of title to be borne and paid for by the second party; with the proviso that it is mutually understood and agreed that the second party shall not make payment of any moneys due under this agreement until the above specified deed and bill of sale and certificate of title has been furnished by the first party to the second party as provided herein

IX.

It is also mutually understood and agreed that a membership in the Lakeside Golf Club, so-called, shall be the sole and separate property of the second party and the first party hereby waives any community property and/or separate property interest therein.

X.

With reference to community property securities, stocks, bonds, mortgages, trust deeds, other evidences of indebtedness or choses in action now held by or in the possession of the first party, and to all of which the second party makes a claim of one-half community property interest therein, it is hereby mutually understood and agreed that the

first party hereby represents that of an original amount of such securities of the approximate value of Thirty Five Thousand Dollars ($35,000.00) and consisting of those set forth below and on page 18 of this agreement; [53]

1932				
February 20th	$2,000.00	Brooklyn Edison,	5%	1-1-52
March 23rd	$2,000.00	Southern California Edison,	5%	6-1-54
1933				
April 17th	$5,000.00	Edison Electric Illuminating of Boston	5%	4-15-36
June 2	$3,000.00	Glendale Sewer	5%	3-1-49
June 2	$3,000.00	Los Angeles Harbor	4¾%	9-1-49
June 2	$3,000.00	San Francisco Water	4½%	7-1-49
June 2	$1,000.00	State of Calif. Veterans Welfare	4%	2-1-46
June 2	$1,000.00	State of Calif. Veterans Welfare	4%	2-1-45
June 24	$5,000.00	State of Calif. Park	4%	1-2-47
		(G.M.S. L.F.M. G.J.S. H.F.N.)		
	$10,000.00	U. S. Government	3½%	1941
		(G.M.S. L.F.M. G.J.S. H.F.N.)		

[54]

there now remains in her possession, control or transferred to anyone for her benefit or that of the minor child of the parties the following securities of the approximate value of Twenty-One Thousand Dollars ($21,000.00) and consisting of:

$3,000.00 Glendale Sewer 5% 3-1-49
$3,000.00 Los Angeles Harbor 4¾% 9-1-49
$3,000.00 San Francisco Water, 4½% 7-1-49
$1,000.00 State of Calif. Veterans Welfare 4% 2-1-46
$1,000.00 State of Calif. Veterans Welfare 4% 2-1-45
$5,000.00 State of Calif. Park 4% 1-2-47
$5,000.00 U. S. Government 3½% 1941

(G.M.S. L.F.M. G.J.S. H.F.N.)

[55]

and the first party hereby represents that other than the last recited securities there do not remain any other of said securities and/or that there has not been transferred to any person or corporation or partnership any of the original amount of said securities or the proceeds of any of the same to be held for the benefit of the first party or of the minor child of the parties, and that there are not any other securities, stocks, bonds, mortgages, trust deeds, other evidences of indebtedness or choses in action which have been purchased with community funds of the parties and that are now held by the first party and or by any person or corporation or partnership for the benefit of the first party or of the minor child of the parties other than those recited above as still remaining of the original amount of the approximate value of Thirty-Five Thousand Dollars ($35,000.00); and as to the above recited and so represented securities now remaining the second party hereby waives and releases in favor of the first party any claim he may have from any

cause whatsoever, it being understood that certain securities, i. e., 100 (one-hundred) Shares of Security Bank Stock and 100 (One Hundred) Shares of Anoconda Copper Stock and 200 (Two Hundred) Shares of Radio Stock and 25 (Twenty-Five) Shares of Oliver Farm Equipment Stock, are specifically released as being the separate property of the first party.

XI.

All taxes, assessments, debts, liens or encumbrances upon any of the real or personal properties disposed of herein and existing at the time of the transfer thereof by either party to the other party or arising thereafter, save and except that the first party warrants that she has not encumbered or sold any of the furniture transferred under this agreement to the second party, shall be borne and paid by the party to whom the properties are transferred hereunder, provided and except that the first party agrees to transfer real property and furniture covered herein to the second party [56] free and clear of all taxes, assessments, debts, liens or encumbrances other than excepted herein, and agrees to assume payment of and pay the same if any exists at the time of the transfer of said properties.

XII.

Hereafter income tax assessments and/or payments assessed, due, paid or payable anywhere upon the gross income and/or the net income of the first party are to be borne and paid for solely by the first party and not by the second party.

XIII.

In the event any income tax payment or payments and penalty or penalties upon income tax payments and/or assessments become due or payable upon the income of the second party or upon the community property income of the first party and the second party as to income for any period or periods during the period of the existence of the marriage of the parties hereto and prior to the execution of this agreement, the parties hereto shall each bear and pay one-half thereof.

XIV.

The first party hereby expressly waives and releases any right or claim the first party may have or now or subsequently claim to have to attorney's fees or costs of action against the second party arising out of legal services rendered to the first party in any action instituted by either party against the other prior or subsequent to the execution of this property settlement or to attorney's fees for legal services rendered to the first party or for fees for investigations services rendered to the first party in connection with any claim or claims either in law, equity or probate and valid or invalid against the second party by the first party and arising or made prior to or subsequent to the signing and execution of this property settlement agreement, or arising at the time of the execution and signing of this property settlement agreement. **[57]**

XV.

Each party hereto hereby expressly waives any right, title interest or any claim or claims he or she may have to the wearing apparel, personal jewelry, personal ornaments, radios, personal furniture or personal effects of the other party.

XVI.

All automobiles now registered in the name of either party shall be the property of and/or remain the property of the party hereto in whose name they are now registered, and each party hereby expressly waives and releases any claim and/or claims, right, title, and/or interest, or community property interest and/or separate property interest either may have or claim to have in such automobiles so registered.

XVII.

It is further mutually understood and agreed that each of the parties may for themselves, independently of the other, control or do business in all matters the same as though he or she were single.

XVIII.

It is further understood and agreed that in making this final settlement of property rights that each of the parties hereto waives, relinquishes and forever surrenders all claim or claims of every kind or nature which she or he has or might hereafter acquire in or to or against the property of the other now held or hereafter acquired, including the rights

of inheritance in case of death intestate or testate, which right each hereby expressly waives in favor of the heirs of the other.

XIX.

It is further mutually understood and agreed that each of the parties hereto, their respective heirs, executors, administrators or assigns, shall, at any and all times, execute any paper that may be necessary to be executed for the purpose of giving full force and effect to these presents and to the covenants, provisions and agreements herein contained.

[58]

XX.

It is further distinctly and expressly understood by and between the respective parties hereto that they and each of them have consulted their attorneys and each fully understands his or her full rights under this agreement and each hereby expresses himself and herself as fully understanding the same and all of the conditions and provisions of this Agreement or Indenture, and with that full understanding, they each for themselves voluntarily execute the same.

XXI.

It is further mutually understood and agreed that as to cash in the possession of the second party and on deposit the first party hereby waives any and all claim and/or claims to an amount of None ($None) either as to her community property rights and/or her separate property rights, and releases the same

to the second party or to the payees of certain checks, it being represented by the second party that there are checks in about that amount against the accounts of the second party and outstanding.

GERTRUDE MARTHA SOMERVILLE
Party of the First Part

Approved:

ARTHUR C. MILLER
Atty. for Party of the First Part
GEO. J. SOMERVILLE
Party of the Second Part
ROBT. G. WHEELER
Atty. for Party of the Second Part

(Acknowledgments of the Parties to Their Signatures Attached)

Approval by the Court

The above property settlement agreement is this .....day of ....., 1936, hereby approved by the Court.

.....
Judge of the Superior Court [59]

State of California,
County of Los Angeles—ss.

On this 1st day of September, 1936, before me L. F. Malone, a Notary Public in and for said County and State, personally appeared Gertrude Somerville, known to me to be the person whose

name is subscribed to the within instrument and acknowledged to me that she executed the same, to-wit;—a Property Settlement Agreement dated September 1st, 1936.

In Witness Whereof, I have hereunto set my hand and affixed my official seal the day and year first above written in this certificate.

[Seal] L. F. MALONE,
Notary Public in and for said County and State.

My commission expires: July, 1938.

State of California,
County of Los Angeles—ss.

On this 2nd day of Sept., 1936, before me Hugh F. Neuhart, a Notary Public in and for said County and State, personally appeared Geo. J. Somerville, known to me to be the person whose name is subscribed to the within instrument and acknowledged to me that he executed the same, to-wit;—a Property Settlement Agreement dated September 1st, 1936.

In Witness Whereof, I have hereunto set my hand affixed my official seal the day and year first above written in this certificate.

[Seal] HUGH F. NEUHART,
Notary Public in and for Said County and State.

My commission expires: June 12, 1940. [60]

FORM 1040
TREASURY DEPARTMENT
INTERNAL REVENUE SERVICE

INDIVIDUAL INCOME TAX RETURN

FOR NET INCOMES FROM SALARIES OR WAGES OF MORE THAN $5,000 AND INCOMES FROM BUSINESS, PROFESSION, RENTS, OR SALE OF PROPERTY

For Calendar Year 1936

or fiscal year begun ....., 1936, and ended ....., 1937

File This Return Not Later Than the 15th Day of the Third Month Following the Close of the Taxable Year

PRINT NAME AND ADDRESS PLAINLY BELOW (See Instruction 25)

GEO. J. SOMERVILLE
(Name) (Both husband and wife, if this is a joint return)

1830 Strand
(Street and number, or rural route)

Hermosa Beach (Post office) Los Angeles (County) Calif. (State)

COPY TO BE RETAINED BY TAXPAYER

IF YOU NEED ASSISTA
IN PREPARING THI
RETURN, GO TO A
DEPUTY COLLECTO
OR TO THE
COLLECTOR'S OFFI

1. State whether you are (a) a citizen of the United States, or (b) a resident alien — a
2. If you filed a return for the preceding year, to which Collector's office was it sent? — Los Angeles
3. Were you married and living with husband or wife during your taxable year? — no
4. Is this a joint return of husband and wife (see Instruction 21)? — no
5. State name of husband or wife if a separate return was made and the Collector's office to which it was sent — Los Angeles
   no. J. Somerville
6. If not married, were you the head of a family (see Instruction 22 for definition) during your taxable year?
7. How many dependent persons (other than husband or wife) under 18 years of age or incapable of self-support received their chief support from you during your taxable year? — One
8. If your status in respect to question 3, 6, or 7 changed during the year, state date and nature of change
9. State whether your books are kept on cash or accrual basis — Cash
10. State principal occupation or profession — Actor
11. Did you transfer to or receive from any one person money or property in excess of $5,000, during the calendar year 1936, without an adequate and full consideration in money or money's worth? — no
    If so, did you file a gift tax return on Form 709 or an information return on Form 710? (Answer "yes" or "no")
12. Did any person or persons advise you in respect of any or matter affecting any item or schedule of this return or advise you in the preparation of this return, or act pare this return for you? (Answer "yes" or "no") If so, — yes
    name and address of such person or persons and nature and extent of the assistance or advice receiv and the items or schedules in respect of which the ass advice was received; if this return was actually pr any person or persons other than yourself, state the the information reported in this return and the n which it was furnished to or obtained by such pers — H.D.Emerson, Hollywo
    Ppd.from taxpayers info
13. Did you make a return of information on Forms 1066 and 1099 (see Instruction 21) for the calendar year 1936? (Answer "yes" or "no")

Item and Section No.	INCOME (State name and address of employer)	Amount received	Expenses paid (Deductible in Schedule F)
	Salaries, Wages, Commissions, Fees, etc. SCHEDULE ATTACHED	$ 30 720 23	$
2.	Net Profit (or Loss) from Business or Profession. (From Schedule A)		
3.	Interest on Bank Deposits, Notes, Corporation Bonds, etc. (except interest on tax-free covenant bonds). (State kind of business) (Attach detailed statement)	133 93	
4.	Interest on Tax-free Covenant Bonds Upon Which a Tax was Paid at Source. (Attach detailed statement)		
5.	Taxable Interest on Government obligations, etc. (From Schedule D, Line (g))		
6.	Dividends. (From Schedule E)		
7.	Income (or Loss) from Partnerships, Syndicates, Pools, etc. (Furnish name, address, and kind of business)		
8.	Income from Fiduciaries. (Furnish name and address)		
9.	Rents and Royalties. (From Schedule B)		
10.	Capital Gain (or Loss). (From Schedule C) (If capital loss, this amount may not exceed $2,000)		
11.	Other Income. (State nature.) (Use separate schedule, if necessary)		
12.	TOTAL INCOME IN ITEMS 1 TO 11		$ 30 854
	DEDUCTIONS		
13.	Interest Paid. (Explain in Schedule F)	$ 1 181 66	
14.	Taxes Paid. (Explain in Schedule F)		
15.	Losses by Fire, Storm, etc. (Explain in table at foot of page 2)		
16.	Bad Debts (including bonds determined to be worthless during taxable year). (Explain in Schedule F)		
17.	Contributions. (Explain in Schedule F) Schedule attached	312 66	
18.	Other Deductions Authorized by Law (including stock determined to be worthless during taxable year). (Explain in Schedule F)		
19.	TOTAL DEDUCTIONS IN ITEMS 13 TO 18		1 494
20.	NET INCOME (Item 12 minus Item 19)		$ 29 359

COMPUTATION OF TAX (See Instruction 23)

21.	Net income (Item 20 above)			$	29	359	84	$ 1 062
22.	Less: Personal exemption	$	1000 00					2 612
23.	Credit for Dependents. (Explain in Schedule F)		400 00		1	400	00	$ 3 674
24.	Balance (Surtax net income)			$	27	959	84	
25.	Less: Interest on Government obligations, etc. (Item 5)	$						
26.	Earned income credit. (See Instruction 22)		1400 00		1	400	00	
27.	Balance subject to normal tax			$	26	559	84	

28.	Normal tax (4% of Item 27)	$	1 062
29.	Surtax on Item 24. (See Instruction 23)		2 612
30.	Total tax. (Item 28 plus Item 29)	$	3 674
31.	Less: Income tax paid at source (2% of Item 4)	$	
32.	Income tax paid to a foreign country or U. S. possession		
33.	Balance of Tax. (Item 30 minus Items 31 and 32)	$	3 674

TAXPAYER'S RECORD OF PAYMENTS

PAYMENT	AMOUNT	DATE	CHECK OR M. O. No.	BANK OR OFFICE OF ISSUE
First	$			
Second				
Third				
Fourth				

An amended return must be marked "Amended" at top of return. Checks and drafts will be accepted only if payable at par.

Schedule A—Profit (or Loss) From Business or Profession—[Not filled in]

Schedule B—Income From Rents and Royalties—[Not filled in]

Schedule C—Capital Gains and Losses (From Sales or Exchanges Only)—[Not filled in]

Schedule D—Interest on Government Obligations, etc.—[Not filled in]

Schedule E — Income From Dividends — [Not filled in]

Schedule F—Explanation of Deductions Claimed in Items 1, 13, 14, 16, 17, and 18, and Credit Claimed in Item 23-4-L. A. & Orange Co. Real Estate 445.00 ½ each 222.50 Calif. Income tax $959.16.

Explanation of Deduction for Depreciation Claimed in Schedules A and B—[Not filled in]

Explanation of Deduction for Losses by Fire, Storm, etc., Claimed in Schedule A and in Item 15—[Not filled in] [62]

INCOME TAX RETURN—1936

GEO. J. SOMERVILLE

(Known as Slim Summerville)

1830 Strand, Hermosa Beach, Calif.

Item 1

Income:			
20th Century-Fox Hollywood			$69,062.50
Expense:			
Agents commission		$6,906.25	
Accounting		125.00	
Wardrobe	$327.23		
50% business		163.62	
Advertising		149.25	
Trade papers		16.00	
Dues		5.00	
Fan photos		35.25	
Photo mailers & postage (est'd.)		25.00	
Auto Expense—			
Cost 1934	$453.38		
Depreciation	$113.35		
Insurance	100.00		
Operation	180.00		
	$393.35		
50% business		196.67	7,622.04
			$61,440.46

George J. Somerville $30,720.23

Mrs. George J. Somerville $30,720.23

Item 17

Childrens Home Society	$175.00
Salvation Army	10.00
Red Cross	25.00
Old Age Sheltering Home	5.00
L. A. Orthopaedic Hospital	25.00
L. A. Tuberculosis Assn.	15.00
Relief Guild	25.00
Motion Picture Relief	345.32
	$625.32

George J. Somerville	$312.66
Mrs. George J. Somerville	$312.66

[63]

EXHIBIT "E"

937 UNITED STATES 1937

INDIVIDUAL INCOME TAX RETURN

Do not write in this space

Treasury Department Internal Revenue Service
(Form 1040)

Do not use these spaces

(Auditor's Stamp)

For Net Incomes From Salaries, Wages, Interest, and Dividends of More Than $5,000, and Incomes From Other Sources Regardless of Amounts

File Code

Serial Number

For Calendar Year 1937 or Fiscal Year beginning....., 1937, and ended....., 1938

District

(Cashier's Stamp)

File this return not later than the 15th day of the third month following the close of the taxable year

Print Name and Aldress Plainly
(See Instruction E)

GEORGE SOMERVILLE
3425 Hermosa Avenue
Hermosa Beach Los Angeles Calif.

Cash—Check
M. O.
First Payment.

Item and struction No.

INCOME Schedule attached

1. Salaries and other compensation for personal services (from Schedule A)..... $47,860.97
2. Dividends from domestic and foreign corporations 175.75
3. Interest on bank deposits, notes, mortgages, etc. 357.02
4. Interest on corporation bonds..... .....
5. Taxable interest on Government obligations, etc. (from Schedule B)..... .....
6. Income (or loss) from partnerships, syndicates, pools, etc. (furnish name and address):
....

INCOME Schedule attached

7.	Income from fiduciaries (furnish name and address):		
8.	Rents and royalties (from Schedule C)		
9.	Income (or loss) from business or profession (from Schedule D)		
10.	Gain (or loss) from sale or exchange of property (from Schedule F)		
11.	Other income (state nature; use separate schedule if necessary)		
12.	Total income in items 1 to 11 (enter non-taxable income in Schedule H)		$48,393.74

DEDUCTIONS

13.	Contributions (explain in Schedule G) Schedule attached	$ 400.00	
14.	Interest (explain in Schedule G)		
15.	Taxes (explain in Schedule G) Schedule attached	1,527.78	
16.	Losses by fire, storm, etc. (explain in Schedule G)		
17.	Bad debts (explain in Schedule G)		
18.	Other deductions authorized by law (explain in Schedule G)		
19.	Total deductions in items 13 to 18		1,927.78
20.	Net income (item 12 minus item 19)		$46,465.96

COMPUTATION OF TAX

21.	Net income (item 20 above)		$46,465.96
22.	Less: Personal exemption (from Schedule I)	$1,125.00	
23.	Credit for dependents (from Schedule I)		1,125.00

24.	Balance (surtax net income)		$45,340.96
25.	Less: Interest on Government obligations (item 5)	$	
26.	Earned income credit (from Schedule J)	$1,400.00	1,400.00
27.	Balance subject to normal tax		$43,940.96
28.	Normal tax (4% of item 27)		$ 1,757.64
29.	Surtax on item 24 (see Instruction 29)		6,442.06
30.	Total tax (item 28 plus item 29)		$ 8,199.70
31.	Less: Income tax paid at source	$	
32.	Income tax paid to a foreign country or U. S. possession		
33.	Balance of tax (Item 30 minus items 31 and 32)		$ 8,199.70

Note.—One form marked "Duplicate Copy" must be filed with this original return ($5 will be assessed if duplicate copy is not filed)

[64]

Schedule A.—Income From Salaries and Other Compensation for Personal Services.—[Not filled in]

Schedule B.—Interest on Government Obligations, Etc.—[Not filled in]

Schedule C.—Income From Rents and Royalties.—[Not filled in]

Schedule D.—Profit (or Loss) From Business or Profession.—[Not filled in]

Schedule E.—Explanation of Deduction for Depreciation Claimed in Schedules C and D.—[Not filled in] [65]

INCOME TAX RETURN—1937

GEORGE SOMERVILLE
(Slim Summerville)
3423 Hermosa Avenue
Hermosa Beach, Calif.

Item I—Period 1-1-37 to Date of Divorce 10-2-37

Twentieth Century Fox			$65,618.10
Expense:			
Unemployment tax		$ 590.56	
Agents commission		6,561.81	
Advertising		168.53	
Trade papers		16.00	
Dues		75.00	
Miscellaneous		25.00	
Fan photos		50.00	
Accounting		100.00	
Auto Expense:			
Deprec. 25%	$453.38	$ 85.01	
Insurance		75.00	
Operation		135.00	
		$295.01	
50% business		147.50	7,734.40
			$57,883.70
George Somerville		$28,941.85	
Gertrude Somerville		$28,941.85	

[66]

INCOME TAX RETURN—1937

GEORGE SOMERVILLE
(Slim Summerville)
3423 Hermosa Avenue
Hermosa Beach, Calif.

Item I—Period 10-2-37 to 12-8-37 (Single)			
Twentieth Century Fox			$18,000.00
Expense:			
Unemployment tax		$ 162.00	
Agents commission		1,800.00	
Dues		25.00	
Miscellaneous		25.00	
Auto Expense:			
Deprec. 25% (2 mo.)	$453.38	$18.90	
Insurance		16.63	
Operation		30.00	
		$65.53	
50% business		32.77	2,044.77
			$15,955.23

Recap Item (1) 1st Period	$28,941.85	
Item (2) 2nd Period	15,955.23	
Item (3) 3rd Period	2,963.89	
	$47,860.97	
Item 13		
Community Chest		$ 250.00
Red Cross		50.00
Childrens Home		50.00
L. A. Orthopaedic Society		50.00
		$400.00

Item 15	
Real Estate	$ 542.64
State Income	985.14
	$1,527.78

[67]

INCOME TAX RETURN—1937

GEORGE SOMERVILLE
(Slim Summerville)
3423 Hermosa Avenue
Hermosa Beach, Calif.

Item I—Period subsequent to marriage December 8, 1937

Twentieth Century Fox			$6,666.67
Expense:			
Unemployment tax		$ 60.00	
Agents commission		666.67	
Auto Expense:			
Deprec. 25% (1 mo.)	$453.38	$ 9.45	
Operation		15.00	
		$24.45	
50% business		12.22	738.89
			$5,927.78

George Somerville	$2,963.89
Eleanore L. Somerville	$2,963.89

[68]

Schedule F.—Gains and Losses From Sales or Exchanges of Property.—[Not filled in.]

Schedule G.—Explanation of Deductions Claimed in Items 13, 14, 15, 16, 17, and 18—[Not filled in]

[69]

Schedule H.—Nontaxable Income Other Than Interest Reported in Schedule B.—[Not filled in]

Schedule I.—Explanation of Credits Claimed in Items 22 and 23. (See Instructions 22 and 23)

(a) Personal Exemption

Status	Number of Months During Year in Each Status	Credit Claimed
Single, or married and not living with husband or wife	11	$ 916.67
Married and living with husband or wife	1	208.33
Head of family (explain below)	.....	1,125.00
Reason for credit		
Name of dependent and relationship		

(b) Credit for Dependents—[Not filled in]

Schedule J.—Computation of Earned Income Credit. (See Instruction 26)

(a) For Net Income of $3,000, or Less—[Not filled in]

(b) For Net Income in Excess of $3,000

1.	Earned net income (Not over $14,000)	$14,000.00
2.	Net income (item 20, page 1)	46,465.96
3.	Earned income credit (10% of line 1 or 2, above, whichever amount is smaller, but do not enter less than $300)	1,400.00

QUESTIONS

1. State your principal occupation or profession—Actor
2. Check whether you are a citizen [X] or resident alien [ ]
3. If you filed a return for the preceding year, to which Collector's office was it sent?—Los Angeles
4. Are items of income or deductions of both husband and wife included in this return? (See Instruction B—no
5. State name of husband or wife if a separate return was made and the Collector's office to which it was sent—Los Angeles. Eleanor Somerville and Gertrude Somerville
6. Check whether this return was prepared on the cash [ ] or accrual [ ] basis.
7. Did you at any time during your taxable year own directly or indirectly any stock of a domestic or foreign personal holding company? (Answer "yes" or "no")—no. If answer is "yes", attach schedule required by Instruction M.

AFFIDAVIT. (See Instruction F)

I/we swear (or affirm) that this return (including any accompanying schedules and statements) has been examined by me/us, and to the best of my/our knowledge and belief is a true, correct, and complete return, made in good faith, for the taxable year stated, pursuant to the Revenue Acts of 1936 and 1937 and the regulations issued thereunder.

GEORGE SOMERVILLE

If this is a joint return (not made by agent) it must be signed by both husband and wife and sworn to before a proper officer by the spouse preparing the return, or if neither or both prepare the return then by both spouses.

Subscribed and sworn to by George Somerville before me this 14th day of March, 1938.

URSULA SITAR,
Notary Public.

My Commission Expires Jan. 16, 1940.

A return made by an agent must be accompanied by power of attorney. (See Instruction F.)

AFFIDAVIT. (See Instruction F)

(If this return was prepared for you by some other person, the following affidavit must be executed)

I/we swear (or affirm) that I/we prepared this return for the person or persons named herein and that the return (including any accompanying schedules and statements) is a true, correct, and complete

statement of all the information respecting the income-tax liability of the person or persons for whom this return has been prepared of which I/we have any knowledge.

H. D. EMERSON
(Signature of person preparing the return)
BOYLE & WOOD
(Name of firm or employer, if any)

Subscribed and sworn to before me this 14th day of March, 1938.

URSULA SITAR,
Notary Public.
(Signature and title of officer administering oath)

My Commission Expires Jan. 18, 1940. [70]

[Title of Board and Cause.]

STIPULATION

It Is Hereby Stipulated by and between the parties hereto, through their respective counsel, that the foregoing Statement of Facts and Evidence and the foregoing Stipulation, with Exhibits attached thereto, constitute a statement of all of the material evidence introduced at the hearing before the United States Board of Tax Appeals and the same is approved by the undersigned, as attorneys for Petitioner on review, and by the undersigned, Chief

Counsel for the Bureau of Internal Revenue, as attorney for the Commissioner of Internal Revenue, Respondent on review.

Dated this 12th day of June, 1941.

EDWARD L. CONROY,
DON CONROY,
Attorneys for Petitioner on Review.

J. P. WENCHEL,
Chief Counsel for the Bureau of Internal Revenue.

[Endorsed]: U. S. B. T. A. Filed June 12, 1941.

[71]

[Title of Board and Cause.]

PRAECIPE FOR TRANSCRIPT

To the Clerk of the United States Board of Tax Appeals:

You will please prepare, transmit and deliver to the Clerk of the United States Circuit Court of Appeals, for the Ninth Judicial Circuit, copies, duly certified as correct, of the following documents and records in the above entitled cause, in connection with the Petition for Review by the said Circuit Court of Appeals, for the Ninth Judicial Circuit, heretofore filed by the above named Petitioner:

1. Docket entries of the proceedings before the Board.

2. Petition filed on May 29, 1939, and Answer filed on July 26, 1939.

3. Findings of Fact and Opinion of the Board promulgated on March 14, 1941, and decision entered March 14, 1941.

4. Petition for Review filed on June 3, 1941. [72]

5. Notice of filing Petition for Review, filed on June 3rd, 1941.

6. Statement of Evidence approved and filed on June 12, 1941.

7. This Praecipe for record.

8. Notice of filing this Praecipe and the admission of service thereof.

Said transcript to be prepared as required by law and the Rules of the United States Circuit Court of Appeals, for the Ninth Judicial Circuit.

EDWARD L. CONROY,
DON CONROY,
Attorneys for Petitioner.

Service of a copy of this Praecipe is hereby admitted this 12th day of June, 1941. Agreed to.

J. P. WENCHEL,
Chief Counsel, Bureau of Internal Revenue, Counsel for Respondent.

[Endorsed]: U.S.B.T.A. Filed June 12, 1941.

[73]

[Title of Board and Cause.]

NOTICE OF FILING OF PRAECIPE

To:

J. P. Wenchel, Attorney for Respondent, Chief Counsel, Bureau of Internal Revenue, Internal Revenue Building, Washington, D. C.

Please take notice that on the 12th day of June, 1941, the undersigned, attorneys for George J. Somerville, (Also known as Slim Summerville) the Petitioner in the above entitled proceeding, has filed with the Clerk of the United States Board of Tax Appeals a Praecipe for Record, a copy of which is annexed hereto.

Dated: June 12th, 1941.

EDWARD L. CONROY,
DON CONROY,
Attorneys for Petitioner.

Receipt of the foregoing Notice of filing the Praecipe for Record and service of a copy of the Praecipe herein mentioned is acknowledged this 12th day of June, 1941.

(Signed) J. P. WENCHEL,
Chief Counsel, Bureau of Internal Revenue, Attorney for Respondent.

[Endorsed]: U.S.B.T.A. Filed June 12, 1941. [74]

[Title of Board and Cause.]

CERTIFICATE

I, B. D. Gamble, clerk of the U. S. Board of Tax Appeals, do hereby certify that the foregoing pages, 1 to 74, inclusive, contain and are a true copy of the transcript of record, papers, and proceedings on file and of record in my office as called for by the Praecipe in the appeal (or appeals) as above numbered and entitled.

In testimony whereof, I hereunto set my hand and affix the seal of the United States Board of Tax Appeals, at Washington, in the District of Columbia, this 20th day of June, 1941.

(Seal) B. D. GAMBLE,
Clerk, United States Board of Tax Appeals.

[Endorsed]: No. 9857. United States Circuit Court of Appeals for the Ninth Circuit. George J. Somerville, also known as Slim Summerville, Petitioner, vs. Commissioner of Internal Revenue, Respondent. Transcript of the Record upon Petition to Review a Decision of the United States Board of Tax Appeals.

Filed July 1, 1941.

PAUL P. O'BRIEN,
Clerk of the United States Circuit Court of Appeals for the Ninth Circuit.

United States Circuit Court of Appeals
Ninth Judicial Circuit

No. 9857

GEORGE J. SOMERVILLE,
(Also known as Slim Summerville)
Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

DESIGNATION OF RECORD TO BE PRINTED ON REVIEW AND STATEMENT OF THE POINTS UPON WHICH PETITIONER RELIES ON APPEAL.

To Paul P. O'Brien, Clerk of the Above Entitled Court:

The Petitioner, George J. Somerville, also known as Slim Summerville, through his counsel, Edward L. Conroy and Don Conroy, does hereby notify you that he desires to have printed the entire record on review in the above entitled matter, as certified to you by the Clerk of the United States Board of Tax Appeals.

The points upon which Petitioner relies on appeal are the same as set forth in the Assignment of Errors in the Petition for Review filed with the United States Board of Tax Appeals.

Dated: July 15, 1941.

EDWARD L. CONROY,
DON CONROY,
Counsel for Petitioner.

AFFIDAVIT OF SERVICE BY MAIL

State of California,
County of Los Angeles.—ss.

Harriette Michael, being first duly sworn, deposes and says: that affiant is a citizen of the United States and a resident of the County of Los Angeles; that affiant is over the age of eighteen years and is not a party to the within and above entitled action; that affiant's business address is 1680 North Vine Street, Los Angeles, California; that on the 15th day of July, 1941, affiant served the within Designation of Record to be Printed on Review and Statement of the Points upon Which Petitioner Relies on Appeal on the Respondent in said action by placing a true copy thereof in an envelope addressed to the attorney of record for said Respondent at the office address of said attorney as follows:

J. P. Wenchel, Chief Counsel
Bureau of Internal Revenue
Washington, D. C.

and by then sealing said envelope and depositing the same, with postage thereon fully prepaid, in the United States Post Office at Los Angeles, California, where is located the office of the attorneys for the person by and for whom said service was made.

That there is delivery service by the United States mail at the place so addressed and there is

a regular communication by mail between the place of mailing and the place so addressed.

HARRIETTE MICHAEL.

Subscribed and sworn to before me this 15th day of July, 1941.

EDWARD L. CONROY,
Notary Public in and for said County and State.

[Endorsed]: Filed July 16, 1941. Paul P. O'Brien, Clerk.

No. 9857.

IN THE

United States Circuit Court of Appeals

FOR THE NINTH CIRCUIT

GEORGE J. SOMERVILLE, also known as SLIM SOMERVILLE,
Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

PETITIONER'S OPENING BRIEF.

EDWARD L. CONROY,
DON CONROY,
501 Taft Building, Los Angeles,
Attorneys for Petitioner.

Parker & Baird Company, Law Printers, Los Angeles.

TOPICAL INDEX.

TABLE OF AUTHORITIES CITED.

CASES.

STATUTES.

No. 9857.

IN THE

United States Circuit Court of Appeals

FOR THE NINTH CIRCUIT

GEORGE J. SOMERVILLE, also known as SLIM SOMERVILLE,
Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

PETITIONER'S OPENING BRIEF.

Jurisdictional Statement.

This is an appeal from an order of the United States Board of Tax Appeals, affirming the action of the Commissioner of Internal Revenue in determining deficiencies of income tax due from petitioner for the calendar years 1936 and 1937 in the respective amounts of $3,588.01 and $11,229.22. [R. 24.]

On March 15, 1939, in accordance with the provisions of Section 272A of the Internal Revenue Code, the Commissioner of Internal Revenue, respondent herein, notified petitioner that the determination of petitioner's income tax liability for the years 1936 and 1937 disclosed a deficiency of $14,817.23 [R. 6], of which amount $3,588.01 was deficiency for the year 1936 [R. 9] and $11,229.22

was deficiency for the year 1937 [R. 11]. From these determinations petitioner duly filed his appeal to the United States Board of Tax Appeals in accordance with the provisions of Section 272A of the Internal Revenue Code, and said appeal was given docket number 98831.

The appeal was called for hearing by the United States Board of Tax Appeals on June 10, 1940, at Los Angeles, California [R. 2]. Stipulation of facts was filed at said hearing [R. 34] and said stipulation contained all of the evidence to be presented and the appeal was submitted to the Board of Tax Appeals for decision [R. 2].

On March 14, 1941, the Board of Tax Appeals promulgated its findings of fact and opinion in said appeal [R. 12-23] and entered its decision and final order determining deficiencies in petitioner's income tax for the year 1936 in the amount of $3,588.01 and for the year 1937 in the amount of $11,229.22 [R. 24].

Petitioner, being an individual, residing in California, and the income tax returns of petitioner having been filed with the Collector of Internal Revenue for the Sixth District of California, at Los Angeles, California, the appeal from the decision and order of the Board of Tax Appeals was brought to this Court. The petition for review was filed on June 3, 1941 [R. 25], pursuant to the provisions of Section 1141 of the Internal Revenue Code.

Statement of Facts.

The facts were stipulated to by the parties and are incorporated in the statement of evidence approved by the Board as a part of the record of this appeal [R. 31 *et seq.*] and may be summarized as follows: Petitioner resides in the County of Los Angeles, State of California, and he and his then wife, Gertrude Martha Somerville (hereinafter referred to as "Mrs. Somerville") were residents of the County of Los Angeles, State of California, during the years 1936 and 1937 [R. 35 and 15]; petitioner and Mrs. Somerville were husband and wife for several years prior to 1936 [R. 34] and on September 1, 1936, they entered into a property settlement agreement [R. 34]; the property settlement agreement is set forth in full in the record [R. 41 *et seq.*]; on September 28, 1936, Mrs. Somerville obtained an interlocutory judgment of divorce in the Superior Court of the State of California, in and for the County of Los Angeles [R. 37], and on October 2, 1937, a final judgment of divorce was entered in said divorce proceedings [R. 39]. Petitioner's total net earnings from his personal services for the year 1936 were $61,440.46, one-half of which was reported on the income tax return of petitioner and one-half of which was reported on the income tax return of Mrs. Somerville [R. 35]; that from the date of the property settlement agreement, namely, September 1, 1936, to and including December 31, 1936, petitioner's net earnings from his personal services were $28,357.23 [R. 35]; that petitioner's net earnings from his personal services for that part of the year 1937 commencing January 1, and ending October 2 (the latter date being the date of the final judgment of divorce) were $57,883.70, one-half of which was reported on the income tax return filed by petitioner and one-half

of which was reported on the income tax return filed by Mrs. Somerville [R. 36]; and petitioner's total net earnings from his personal services for the year 1937 were $79,766.71 [R. 35].

The deficiencies here in controversy result from respondent's determination that the income of petitioner from September 1, 1936, the date of said property settlement agreement, to October 2, 1937, the date of the final judgment of divorce, was the sole and separate income of petitioner, and that petitioner and Mrs. Somerville were not entitled to file separate income tax returns, each claiming one-half of said income as their respective community shares.

Specifications of Error.

1. The Board of Tax Appeals erred in holding that the income of petitioner from his personal services for that part of the year 1936 commencing September 1 and ending December 31, and his income from his personal services for that part of the year 1937 commencing January 1 and ending October 1 was taxable entirely to petitioner as his sole and separate property.

2. The Board of Tax Appeals erred in holding that the property settlement agreement entered into by petitioner and his then wife, Gertrude Martha Somerville, had the effect of changing the status of his subsequent earnings from community earnings to separate earnings.

Summary of Argument.

The personal earnings of a husband and wife, residents of California, constitute community property under the laws of that state in the absence of an agreement between them to the contrary. Such earnings received subsequent to July 29, 1927, the effective date of Section 161a of the Civil Code of the State of California, are taxable one-half to each spouse for federal income tax purposes.

It is conceded that under California law a husband and wife can alter their respective property rights by contract, thus changing separate property into community property or community property into separate property. In this case the taxpayer and his wife entered into a contract respecting their property, but did not expressly or by implication change the character of petitioner's future earnings. In fact the contract specifically provides that for a period of two years the wife should receive one-half of the net earnings of petitioner.

This Court has held that the wife has an immediate vested interest in one-half of the earnings of the husband and, in the absence of any conveyance or agreement by her, transferring that right to the husband, it would be retained by her and be subject to the tax as her income.

Income is taxed to its owner and the ownership of income in this case depends upon the laws of California and the agreement of the parties made pursuant to those laws. Such agreements must be construed in accordance with the decisions of the appellate courts of California. Before it will be determined that a husband or wife has waived the right to his or her community interest there must be clear and explicit language to that effect and any uncertainty in the language of the agreement will be resolved in favor of the right.

ARGUMENT.

The Agreement Between Petitioner and His Wife Did Not Convert His Personal Earnings Into His Separate Property and, Therefore, Only One-half of His Earnings Are Taxable to Him.

We have heretofore referred to the record establishing that the parties stipulated that petitioner and his wife entered into a property settlement agreement on September 1, 1936, that petitioner's wife obtained an interlocutory judgment of divorce on September 28, 1936, and a final judgment of divorce was entered on October 2, 1937. Therefore petitioner and Gertrude Martha Somerville retained the status of husband and wife until the final judgment of divorce was entered. *Estate of Boeson,* 201 Cal. 36, 255 Pac. 800. In the absence of an agreement to the contrary, the earnings of a husband and wife are community property until the final judgment of divorce is entered. To that effect Section 161A of the Civil Code of the State of California provides:

> "161a. Interests in community property. The respective interests of the husband and wife in community property during continuance of the marriage relation are present, existing and equal interests under the management and control of the husband as is provided in Sections 172 and 172a of the Civil Code. This section shall be construed as defining the respective interests and rights of husband and wife in community property."

The interlocutory judgment of divorce does not dissolve the marriage.

Strupelle v. Strupelle, 59 Cal. App. 526, 211 Pac. 248;

Estate of Fulton, 50 Cal. App. (2d) 202, 59 Pac. (2d) 508.

The determination of this appeal, therefore, resolves itself into one question, namely: Does the property settlement agreement provide that the subsequent earnings of petitioner shall be his sole and separate property? To answer this question we must look to the agreement for the facts and to the California cases for the law interpreting similar agreements made by residents of that state.

In holding that the property settlement agreement changed the nature of petitioner's earnings from community to separate property, the Board of Tax Appeals failed to follow the decisions of the appellate courts of the State of California in so far as those decisions deal with the construction of such agreements. Furthermore, the Board appears to have assumed that *Van Every v. Commissioner,* 108 Fed. (2d) 650, is controlling. The record on appeal in the *Van Every* case establishes that the property settlement agreement involved in that case definitely did change the nature of all property and earnings acquired by either spouse subsequent to its date. The pertinent provisions of that agreement are quoted from pages 56 and 57 of the record on appeal in that case, filed with this Court, and provide as follows:

> "Article XVII. First party hereby releases, remises, grants and forever quitclaims to second party any and all right, title or interest which he may have or claim to have to any real or personal property possessed by second party, or standing in second party's name, and to any and all property received or

to be received by her under the terms of this agreement, and likewise to any and all estate and property which second party may acquire hereafter, in any manner whatsoever, to the end that all property heretofore or hereunder vested in second party, as well as all property acquired by her in the future, shall be her sole and separate estate, free and clear of any community property or other interest or claim therein, upon the part of first party. First party further releases and discharges second party from any and all claims, demands or obligations to support or maintain him to any extent whatever.

Article XVIII. Second party hereby releases, remises, grants and forever quitclaims to first party all of her right, title, interest and estate, including any community property interest or community property claim, in and to any and all property, whether real or personal, excepting only the real and personal property hereinabove provided to be transferred and conveyed to second party, now belonging to or possessed by or standing in the name of first party, or which first party may hereafter acquire in any manner whatsoever, to the end that all of the property now standing in the name of or belonging to first party, excepting only the property hereinabove provided to be transferred and conveyed to second party, and all property hereafter acquired by him, both real and personal, shall be his sole and separate property and estate, free and clear of any and all community property interest and/or claim upon the part of second party. Second party hereby forever releases and discharges first party from any claim, demand or obligation to support, maintain or provide for her or said minor children in any manner whatsoever, excepting for the payments to be made to her as provided in this agreement."

Furthermore, in the *Van Every* case it was conceded by the taxpayer that an agreement did change the status of their property and future earnings and that such agreements are valid in the State of California. The sole question raised in that case was whether or not such agreements, although valid for all other purposes, affected the tax liability of the husband and wife.

In this case it is petitioner's sole contention that the property settlement agreement did not provide for and therefore did not affect a change in the status of his earnings. Looking to the terms of the agreement, we find that it provides that Mrs. Somerville was to receive one-half of petitioner's net income for two years after its date, which more than covered the period of their marriage. In this connection the agreement states:

> "Now, therefore, for and in consideration of the premises and mutual covenants herein expressed by and between the said parties hereto, the party of the second part agrees to pay to the party of the first part, and the party of the first part agrees to accept, a sum equal to one-half of the net income received by the second party from whatsoever source other than from income received from investments made during said period and other than income received by reason of testate or intestate succession, for a period of two years next and consecutively following upon and from the date of the execution and signing of this property settlement agreement, . . ." [R. 44.]

Comparing the foregoing language with the following language of this Court's opinion in the case of *Sherman v. Commissioner,* 76 Fed. (2d) 810-811:

> "Bearing in mind that the wife has an immediate vested interest in one-half of the earnings of the husband, *in the absence of any conveyance or agreement by her transferring her right to the husband, it would be retained by her and be subject to tax as her income."* (Italics supplied by petitioner.)

it appears that it would be dealing in riddles to say that Mrs. Somerville received one-half of the income and at the same time the same income was *transferred* to her husband. Since she did not alienate or transfer her community one-half interest, it is inescapable, under the holding of *Sherman v. Commissioner, supra,* that she is subject to the income tax imposed upon that income.

Neither should a decision in this case be based upon *Helvering v. Hickman,* 70 Fed. (2d) 985, nor *Sparks v. Commissioner,* 112 Fed. (2d) 774, both of which cases are cited as authority in the Board's opinion. In neither of those cases was there a question as to the construction of the contract, the only question being whether or not agreements similar to the one here involved affected the tax liability of the parties, even though they were effective for all other purposes.

The Contract Involved Was Made by Residents of California Pursuant to Sections 158 and 159 of the California Civil Code and Its Interpretation Is Governed by the Decisions of That State.

The Board set forth in its opinion the following provisions of the property settlement agreement as being those material to a decision of the question involved:

> "Whereas unhappy differences have arisen between said parties by reason whereof the parties hereto from henceforth cannot live happily together, and by reason whereof they are now living separate and apart, and whereas on account of such unhappy differences the parties henceforth must live separate and apart, each from the other, and whereas in view of such facts it is the desire and intent, finally and absolutely of said parties, by this indenture, to settle and forever adjust, and have settled and forever adjusted between themselves, all of their mutual and respective present and future property rights, both as to the properties which either may claim to be community property, and also as to the separate estate of each, . . .
>
> Whereas it is further desired and agreed on the part of the parties hereto, finally and absolutely, to settle and adjust by this indenture all of their mutual and respective rights and obligations one to the other arising out of their marriage relation, and also to determine and settle their respective rights of inheritance one from the other; and
>
> Whereas the said parties hereto have, since the date of their marriage, acquired certain community property; and
>
> Whereas there is a minor child of the parties hereto, and it is their further desire and intent by this inden-

ture to provide for the maintenance, care and custody of said minor child; and

. . . . . .

Now therefore, for and in consideration of the premises and mutual covenants herein expressed by and between the said parties hereto, the party of the second part agrees to pay to the party of the first part, and the party of the first part agrees to accept, a sum equal to one-half of the net income received by the second party from whatsoever source other than from income received from investments made during said period and other than income received by reason of testate or intestate succession, for a period of two years next and consecutively following upon and from the date of the execution and signing of this property settlement agreement, . . .

. . . . . .

It is expressly understood and agreed that the above defined and described one-half of the net income of the second party agreed herein to be payable to the first party by the second party for said two year period, and the other covenants, promises, conveyances and transfers provided for in this agreement, are hereby expressly agreed to be in full and final settlement of any claim or claims of any kind or nature, other than otherwise disposed of in this property settlement agreement, which either party might or could otherwise make against the other party, or the separate estate of the other party, one against the other, whether in law or in equity or in probate; also as and for full satisfaction and settlement or any and all claim or claims of community which either might or could make against the other, . . .

XVII. It is further mutually understood and agreed that each of the parties may for themselves, independently of the other, control or do business in all matters the same as though he or she were single.

XVIII. It is further understood and agreed that in making this final settlement of property rights that each of the parties hereto waives, *relinquishes and forever surrenders all claim or claims of every kind or nature which she or he has or might hereafter acquire in or against the property of the other now held or hereafter acquired,* including the rights of inheritance in case of death intestate or testate, which right each hereby expressly waives in favor of the heirs of the other." (Italics supplied by Board.) [R. 16, 17, 18 and 19.]

We also believe that the foregoing excerpts from said agreement are all that are material for a determination of this case.

It will be noted that there is no provision in the agreement to the effect that the subsequent earnings of each spouse are to be the sole and separate property of the earner. However, the Board was of the opinion that the provisions of the agreement hereinabove quoted, and in particular paragraph XVIII, were sufficient to accomplish a change in the nature of petitioner's earnings. It is apparent that the parties did not intend that the provisions of said paragraph should refer to the one-half which was to be received by Mrs. Somerville. If Mrs. Somerville "relinquished and forever surrendered all claim or claims of every kind or nature which she had or might thereafter acquire in or to or against the property of petitioner then held or thereafter acquired by him" [par. XVII, R. 68]

it follows that she would not have been entitled to receive one-half of his earnings theretofore provided to be received by her. To place a different interpretation upon the agreement would be to argue that the agreement is inconsistent in that she received one-half of petitioner's earnings in one paragraph and it is taken away from her in another.

When the general provisions of a contract are inconsistent with the particular provisions thereof, the latter are controlling. Section 3534 of the Civil Code of the State of California provides that "particular expressions qualify those which are general," and the District Court of Appeal, in *Conover v. Smith,* 83 Cal. App. 227-234 (decided May 20, 1927, hearing in Supreme Court denied July 18, 1927) in quoting from *Scudder v. Perce,* 159 Cal. 429, 114 Pac. 571, held:

> "When general and specific provisions of a contract deal with the same subject matter, the specific provisions, if inconsistent with the general provision, are of controlling force."

Also the Board, in referring to the property settlement agreement, makes the following statement:

> "Its initial inducement clause, *supra,* declares the intent of the parties to be to 'forever settle, and have forever settled and adjusted between themselves all of their mutual and respective *present and future property rights, both as to the properties which either may claim to be community property,* and also as to the separate estate of each.' " (Italics supplied by Board.) [R. 22.]

The inducement clause is a general provision and is controlled by the specific terms of the agreement. In examining the inducement clause, we find that the parties state that the purpose of the agreement is to determine, among other things, their respective rights to property that may be claimed to be community property. The inducement clause did not say that the parties would not thereafter acquire community property. Said clause is followed immediately by the provision which states that Mrs. Somerville is to receive one-half of petitioner's earnings for a period of two years. There is nothing in the law saying that a husband and wife must contract to make all of their property either community or separate and surely they may provide that certain portions shall be community and other portions shall be separate. What occurred in this agreement, as appears by its terms, was that certain of the property was to be retained by each of the parties as the sole and separate property of the one receiving it, but this did not apply to petitioner's earnings.

Biggi v. Biggi, 98 Cal. 35, involved the construction of a property settlement agreement between a husband and wife. Among other things the agreement provided that the wife was to receive one-half of the proceeds from the sale of certain real property. A purchaser was found but the husband refused to execute a conveyance unless he received all of the proceeds from the sale. In the litigation which followed, the trial court determined that the wife had no interest in the property and entered judgment accordingly. On appeal the husband contended that the clause in the agreement providing that the wife "releases and acquits said party of the first part from all and every claim of every character and kind whatsoever to other property, other than said one-half interest in said life

estate, and the one-half of said net proceeds of said sale, as aforesaid," had the effect of conveying to him whatever interest his wife had in the land, and that her rights against him could be founded only on his obligation to pay her one-half of the proceeds of any sale that he might make. In reversing the judgment the Court held:

> "The contention by the respondent that by the aforesaid agreement between the parties, the plaintiff conveyed to the defendant whatever interest she had in the land in question, and that her rights against him are only an obligation on his part to pay her one-half of the proceeds of any sale that he may make, is contrary to a proper construction of the instrument. The provision therein that until the property should be sold the husband should be entitled to its possession and occupancy, and should pay to the plaintiff six dollars per month therefor, and the further provision that 'the parties hereto agree to abide by the judgment of said Vandercook, and to sell said premises for such sum, offered or not, as said Vandercook may determine,' are inconsistent with the proposition that the plaintiff's title to the land passed to the defendant by the instrument, and show that whenever a sale should be made in accordance with its terms, it was to be made by both parties, and that the consent of the plaintiff, as well as of the defendant, was necessary to effect the sale. The clause relied upon by the respondent wherein the plaintiff 'releases and acquits said party of the first part from all and every claim of every character and kind whatsoever to other property, other than said one-half interest in said life estate, and the one-half of said net proceeds of said sale, as aforesaid,' when read in connection with the other portions of the instrument, *and the purposes for which the*

parties recite that they have executed the agreement, must be construed as relating to 'other' property than that enumerated in the instrument, and not as a release of her interest in the property out of whose sale she was to receive one-half of the proceeds." (Italics supplied by petitioner.)

It likewise follows that the provisions of paragraph XVIII of the property settlement agreement hereinabove quoted relate to property *other* than the one-half of petitioner's future earnings that respondent was to receive, and she retained her community interest in his earnings.

We reiterate that the record shows that there was no transfer by Mrs. Somerville of her community interest in petitioner's earnings, and the courts of California have always held that before it will be determined that a property settlement agreement between a husband and wife provides for the waiver of a property right, there must be language of present transfer applying directly to the future as well as existing property. One of the latest cases on this point is *Estate of Hurley,* 28 Cal. App. (2d) 584, 83 Pac. (2d) 61. The facts of that case establish that decedent and her husband entered into a property settlement agreement with respect to their present and future property. The material provisions of said agreement are set forth in the opinion of the Court, and read as follows:

" 'That the first party has real and personal property of her own, standing in her name in Oregon and California, and it is the sense of this agreement that she is to have and retain everything that she

owns in the way of property of all kinds, both real and personal, and the second party agrees, at the time of the signing of this contract, to make and execute a Deed, wherein and whereby he shall convey to the first party whatever interest he may have by way of community interest, or otherwise, in and to: . . .' (Describing certain real property.) 'and shall make any and all other necessary conveyances, documents or instruments whatsoever to carry into effect this agreement.

" 'The second party shall not claim, on and after this date, any interest whatever in any real or personal property, including the California property, belonging to or standing in the name of first party, and the first party shall not claim any interest whatsoever in any real or personal property belonging to and standing in the name of the second party, *and each shall take their respective properties, free and clear of all claim of the other, no matter from what source said claim or claims may arise, and this shall include all property in all States or places.*

" 'This document shall also settle all questions of alimony and any and all money demands that one could make against the other of any kind whatsoever, and the first party waives as against the second party, any and all claims that she has or might have against the second party for failure of the second party to support the first party, and this document shall be and is a complete, final and conclusive property settlement, *and settles every possible demand that one could make against the other.* . . .' " (Italics supplied by petitioner.)

The trial court determined that the foregoing language of the agreement was a sufficient waiver and release on the part of the husband to bar him from inheriting the property of his wife as an heir-at-law and he, therefore, had no right to contest her will. In construing the foregoing language of the agreement and reversing the decision of the lower Court, the Court said:

> "Appellant's first ground of appeal is that the terms of the property settlement admittedly signed by him and his wife were not such as to waive his right to inherit the property of his deceased wife as her heir at law or to bar his opposing the probate of her will. Thus the question is squarely presented whether in the case at bar the terms of the contract constituted a release of all future property rights, including inheritable interests, or whether said contract should be construed as reaching no further than to release all of the respective interests of the parties thereto in the property of the other as living spouses.
>
> "It is not disputed that husband and wife may by appropriate agreement waive their respective inheritable rights in the estate of the other. It is equally well established, however, that the courts will not construe a property settlement between husband and wife as depriving the survivor of inheritance *or other rights growing out of the marital relation, except where there is a clear and unmistakable intention to barter away such rights.* The agreement before us seems to be, as stated therein, 'a property settlement between the parties, settling everything including community property'. It also contains a mutual release of 'alimony and any and all money demands that one could make against the other of any kind whatsoever'. There is no release in terms by either one of claims upon the future acquisitions of the

other, nor, in terms any release by either one upon the estate of the other in case of death." (Italics supplied by petitioner.)

Estate of Andres, 126 Cal. App. 146, 14 Pac. (2d) 566 (decided September 21, 1932, hearing in Supreme Court denied November 17, 1932), involved the interpretation of a property settlement agreement between a husband and wife. The parties had not been divorced and the wife claimed the right to a family allowance from her deceased husband's estate. The executor contested this claim and in defense set up a property settlement agreement which had been entered into by the wife and decedent. The following excerpt from the opinion sets forth the material provisions of the agreement:

> "The agreement referred entirely to property and recited that they desired to separate their property interests, 'in order that each party may have exclusive control and disposition of all property standing in his or her respective name.' Therefore in consideration of the premises and of other good and valuable consideration, and of the sum of $2,350 received by Mrs. Anders 'in full satisfaction for this agreement and *in full settlement of her community rights now or hereafter acquired by her',* she released to her husband, his heirs and assigns forever, 'all the right, title and interest, which said party of the first part now has or may hereafter acquire, *by operation of law or otherwise, in and to all other property, real, personal and mixed, which said party of the second part now owns or has acquired or which he may hereafter acquire or own, or which may now or hereafter stand in his name, whether the same be community property or otherwise.*' " . . .

"In a very recent case the Supreme Court of California had before it an appeal from an order granting a family allowance to the widow of a decedent, where the objection to the allowance was based upon a claim of waiver by virtue of a contract between husband and wife. The court said: 'The sole question presented on the appeal is whether the petitioner waived her right to ask for a family allowance by reason of the above-quoted provision of the property settlement agreement. It is not disputed that the wife may, by her agreement, waive such rights. It is well established, however, that in order to bar a family allowance the intention to waive the right must be clear and explicit, and that any uncertainty in the language of the agreement will be resolved in favor of the right. (*In re Estate of Whitney,* 171 Cal. 750 (154 Pac. 855); *In re Estate of Gould,* 181 Cal. 11 (183 Pac. 146).)' *In re Bidigare's Estate,* 215 Cal. 28 (8 Pac. (2d) 122).)" (Italics supplied by petitioner.)

In determining that the foregoing language did not bar her from obtaining a family allowance the Court said:

"The words 'or otherwise' should not, we think, be held to extend the waiver to a claim for family allowance, but should be held to refer to the claims mentioned in the clause in which they are found, viz., claims between them as husband and wife. *These words used in the agreement, instead of being plain and explicit evidence of waiver, tend to the uncertainty which is not permitted to control in cases of this kind.'* " (Italics supplied by petitioner.)

In *Estate of Bidigare,* 215 Cal. 28, 8 Pac. (2d) 123, the wife was granted a family allowance out of her deceased husband's estate and the executor appealed from the order. It was contended by the executor that the widow had waived her right to a family allowance by the following provisions of a property settlement agreement theretofore entered into by the widow and the decedent:

> "It is hereby agreed that, except as herein specified, each party hereto is hereby released and absolved from any and all obligations and liabilities for the future acts and duties of the other, and that each of said parties hereby releases the other from any and all liabilities, debts or obligations of any kind or character incurred by the other from and after this date, and from any and all claims and demands, including all claims of either party hereto upon the other for support and maintenance as wife or husband, or otherwise, it being understood that this instrument is intended to settle the rights of the parties hereto in all of said respects."

The Court, in determining that the foregoing language was not sufficient to bar the widow from the benefits of the family allowance, held:

> "The sole question presented on the appeal is whether the petitioner waived her right to ask for a family allowance by reason of the above-quoted provision of the property settlement agreement. It is not disputed that the wife may, by her agreement, waive such right. It is well established, however, that in order to bar a family allowance the intention to waive the right must be clear and explicit, and that any un-

certainty in the language of the agreement will be resolved in favor of the right. (*Estate of Whitney,* 171 Cal. 750 (154 Pac. 855); *Estate of Gould,* 181 Cal. 11 (183 Pac. 146).)

"The agreement here in question does not in terms waive or purport to waive any claim as surviving widow, as was the case in *Estate of Yoell,* 164 Cal. 540 (129 Pac. 999). By the agreement each party is released from 'any and all claims and demands including all claims of either party hereto upon the other for support and maintenance as wife or husband, or otherwise'. No provision of the contract suggests that the parties had in contemplation the death of the husband before the entering of the final decree of divorce. The release of claims and demands of one against the other would seem to refer to claims and demands between them as living spouses. The claim of the widow here asserted is against the estate of the decedent and not against him. The words 'or otherwise' should not, we think, be held to extend the waiver to a claim for family allowance but should be held to refer to the claims mentioned in the clause in which they are found, viz., claims between them as husband and wife. These words used in the agreement, instead of being plain and explicit evidence of waiver, tend to the uncertainty which is not permitted to control in cases of this kind."

In *Estate of Shapiro,* 39 Cal. App. (2d) 144, 102 Pac. (2d) 569 (decided May 17, 1940, hearing in Supreme Court denied July 16, 1940), the District Court of Appeal affirmed a judgment of the trial court granting a family allowance to the widow of decedent. It was claimed by the objectors that the widow had waived her right to a

family allowance by entering into an agreement which contained the following provisions:

> "As an integral part hereof, and in consideration of all mutual covenants contained herein, that both parties hereby release each other, waive and relinquish all rights, interest or claims against the other for any alimony, attorney's fees or costs in connection with any possible litigation there may be between them and arising out of, or in connection with their domestic relations, or otherwise, which may happen between them at any time during their married life, including also all rights of inheriting, administration, homestead or otherwise, whatever. . . ."

In discussing the question involved and determining that the above quoted provisions of said property settlement agreement did not have the effect claimed by appellant, the Court said:

> " 'The right of a widow to a family allowance is a personal privilege and she can relinquish it when there are no children (*Estate of Yoell,* 164 Cal. 540 (129 Pac. 999); *Estate of Noah,* 5 Cof. Prob. Dec. 277, affirmed in 73 Cal. 583 (15 Pac. 287, 2 Am. St. Rep. 829) and 88 Cal. 468 (26 Pac. 361)); . . . or she may waive and release it in advance by an antenuptial agreement (*Estate of Yoell, supra*) or by a separation agreement (*Estate of Bidigare,* 215 Cal. 28 (8 Pac. (2d) 122; *Wickersham v. Comerford,* 96 Cal. 433 (31 Pac. 358)), but such a waiver must be certain and intended (*Estate of Bidigare, supra*) . . . Whether the right to demand an allowance has been surrendered is a question of interpretation of the contract or decree set up as a bar to the right. In either case the right should not be held to have been surrendered, except by clear and ex-

plicit language. (*Estate of Bidigare, supra; Estate of Gould,* 181 Cal. 11 (183 Pac. 146); *Estate of Whitney,* 171 Cal. 750 (154 Pac. 855); *Estate of Myers,* 115 Cal. App. 443 (1 Pac. (2d) 1013).)' (11A Cal. Jur. 521 *et seq.*)"

Since the decision was rendered by the Board of Tax Appeals in this case, the case of *Boland v. Commissioner,* 118 Fed. (2d) 622 (9th Circuit) was decided. It may be claimed that the *Boland* case is authority, but the facts of that case show that it is in no way determinative of the issues here involved. In the margin of the opinion portions of the agreement are set forth which establish that the Bolands expressly agreed that the husband's earnings would be his separate property. In that connection the following language is more than ample to support the Court's holding:

" 'The parties hereto also being desirous of settling their respective rights in and to the community property of the parties hereto now existing and of . . . *fixing and determining the character of the property hereafter to be acquired by the parties hereto, and . . . and said party of the second part hereby agrees that the portion of the income of the party of the first part not hereinabove in paragraph (1) hereof assigned to the party of the second part and any proceeds from the investment or reinvestment of said portion of said income shall be and become the separate property of the party of the first part.*' " (Italics supplied by petitioner.)

Furthermore, as it was pointed out by the Court in the following language of that decision, the operative parts of the agreement are inconsistent with the concept of community property:

> *"This evidences a fixed determination to strip any future income of its community character, but the operative parts of the agreement are also inconsistent with the concept of community property. For instance, the agreement provides that petitioner assign twenty-five per cent 'of his income for personal services, * * * and such additional portion * * * as* shall be necessary to make the amount hereby assigned equal to the minimum of Five Hundred Dollars ($500.00) per month * * *.' Under the laws of California 'The respective interests of the husband and wife in community property during continuance of the marriage relation are present, existing and equal interests * * *.' Civil Code Calif. #161a. *The agreement contemplates payment of the $500 a month whether earned or not* (*cf.* Burnet v. Whitehouse, 283 U. S. 148, 151, 51 S. Ct. 374, 75 L. Ed. 916, 73 A. L. R. 1534); *the twenty-five per cent is certainly not a present, existing and equal interest."* (Italics supplied by petitioner.)

Of course, it must be conceded that Mrs. Somerville retained and did not transfer her right to receive one-half of petitioner's earnings during the continuance of the marriage, and that important fact places this case squarely within the holding of *Sherman v. Commissioner, supra,* wherein the Court, at page 811, said:

> Bearing in mind that the wife has an immediate vested interest in one-half the earnings of the husband, in the absence of any conveyance or agreement by her transferring that right to the husband, it

would be retained by her and be subject to tax as her income."

The agreement, being subject to the construction placed on similar agreements by the decisions of the Appellate Courts of California, we believe that the cases cited herein, when applied to the facts, demonstrate that there was no intention on the part of petitioner or his wife to change the nature of petitioner's earnings from community to separate.

In concluding on this question, we can do no better than to quote from the language of the opinion in *Jones v. Lamont,* 118 Cal. 499, 50 Pac. 766, wherein the Court, at page 502, in referring to property settlement agreements between a husband and wife, said:

> "We do not think the courts should come to the aid of these contracts so as to deprive either the husband or wife of the property rights growing out of the married relation, except where there is a clear and unmistakable intention to barter away such rights."

Conclusion.

It is therefore earnestly contended that since, by the terms of the agreement, petitioner's wife did not transfer her community interest in his earnings, but continued to receive the portion thereof given to her by the community property laws of California, the decision of the Board of Tax Appeals is erroneous and should be set aside.

Respectfully submitted,

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No. 9857

In the United States Circuit Court of Appeals for the Ninth Circuit

GEORGE J. SOMERVILLE, ALSO KNOWN AS SLIM SUMMERVILLE, PETITIONER

v.

COMMISSIONER OF INTERNAL REVENUE, RESPONDENT

ON PETITION FOR REVIEW OF DECISION OF THE UNITED STATES BOARD OF TAX APPEALS

BRIEF FOR THE RESPONDENT

SAMUEL O. CLARK, Jr.,
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Special Assistants to the Attorney General.

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BRIEF FOR THE RESPONDENT

OPINION BELOW

The only previous opinion in this case is that of the United States Board of Tax Appeals promulgated March 14, 1941 (R. 12–23), which is reported at 43 B. T. A. 968.

JURISDICTION

This appeal involves federal income taxes for the calendar years 1936 and 1937, in the respective amounts of $3,588.01 and $11,229.22, and is taken from a decision of the United States Board of Tax Appeals entered March 14, 1941 (R. 24). The case is brought to this Court by a petition for review filed by the taxpayer on June 3, 1941 (R. 25–29), pursuant to the

provisions of Sections 1141–1142 of the Internal Revenue Code.

QUESTION PRESENTED

Whether the income received by the petitioner, a resident of California, for personal services rendered during the period from the time he entered into a property-settlement agreement with his wife until she was granted a final decree of divorce is taxable in its entirety to the petitioner as his own income, or whether only one-half of the net income received by him during that period for personal services rendered is taxable to him.

STATUTES INVOLVED

Revenue Act of 1936, c. 690, 49 Stat. 1648:

> SEC. 22. GROSS INCOME.
>
> (a) *General Definition.*—"Gross income" includes gains, profits, and income derived from salaries, wages, or compensation for personal service, of whatever kind and in whatever form paid, or from professions, vocations, trades, businesses, commerce, or sales, or dealings in property, whether real or personal, growing out of the ownership or use of or interest in such property; also from interest, rent, dividends, securities, or the transaction of any business carried on for gain or profit, or gains or profits and income derived from any source whatever. * * *
>
> * * * * *

Civil Code of California (1937):

> SEC. 158. *Husband and wife may make contracts.*—Either husband or wife may enter into any engagement or transaction with the other,

or with any other person, respecting property, which either might if unmarried; subject, in transactions between themselves, to the general rules which control the actions of persons occupying the confidential relations with each other, as defined by the title on trusts.

SEC. 159. *Contract altering legal relations: Separation agreement.*—A husband and wife cannot, by any contract with each other, alter their legal relations, except as to property, and except that they may agree, in writing, to an immediate separation, and may make provision for the support of either of them and of their children during such separation.

SEC. 160. *Consideration for agreement of separation.*—The mutual consent of the parties is a sufficient consideration for such an agreement as is mentioned in the last section.

* * * * *

SEC. 161a. *Interests in community property.*—The respective interests of the husband and wife in community property during continuance of the marriage relation are present, existing and equal interests under the management and control of the husband as is provided in sections 172 and 172a of the Civil Code. This section shall be construed as defining the respective interests and rights of husband and wife in community property.

STATEMENT

This is an appeal from a decision of the United States Board of Tax Appeals (R. 24) sustaining a determination by the Commissioner of Internal Revenue of deficiencies in the federal income tax liability

of the petitioner for the calendar years 1936 and 1937 (R. 6–11).

The facts in this case were stipulated before the Board of Tax Appeals (R. 31–86), and the facts as stipulated were adopted by the Board as its findings of fact (R. 15).

The petitioner is an individual residing at Redondo Beach, California (R. 3, 11), and filed federal income tax returns for the years 1936 and 1937 (R. 72–85) with the Collector of Internal Revenue at Los Angeles, California.

The petitioner and Gertrude Martha Somerville were husband and wife for several years prior to 1936 (R. 34), and during the years 1936 and 1937 the petitioner was a resident of the State of California (R. 35).

On September 1, 1936, the petitioner and his wife entered into a property-settlement agreement (R. 34) which is set out in full in the record (pp. 41–71). On September 28, 1936, an interlocutory decree of divorce was entered in the Superior Court of the State of California, in and for the County of Los Angeles, in a proceeding instituted against the petitioner by his wife (R. 34, 37–39). On October 2, 1937, the same court entered a final decree of divorce in the same proceeding (R. 34, 39–40). The petitioner remarried on December 8, 1937 (R. 35).

During the year 1936 the petitioner received the net amount of $61,440.46 as compensation for personal services rendered by him. Of this amount the sum of $28,357.23 represented his net earnings for the period subsequent to the execution of the property-

settlement agreement by the petitioner and his wife on September 1, 1936. During the year 1937 the petitioner received the net amount of $79,766.71 as compensation for personal services rendered. Of this amount the sum of $57,833.70 represented his net earnings for the period from January 1, 1937, to and including October 1, 1937, before the final decree of divorce was entered in the proceeding instituted against him by his wife (R. 35–36).

In his federal income tax return for the year 1936 (R. 72–75) the petitioner reported as a part of his gross income the sum of $30,720.23, being one-half of the net amount of $61,440.46 received by him during the year as compensation for personal services rendered. The remaining one-half of the petitioner's net earnings in 1936 for personal services rendered was reported in the income tax return filed by his wife for the year 1936 (R. 35, 72).

In his federal income tax return for the year 1937 (R. 76–85) the petitioner reported as a part of his gross income the sum of $47,860.97 as compensation for personal services rendered. This sum consisted of $28,941.85, being one-half of his net income for the period from January 1, 1937, to October 2, 1937, for personal services rendered (R. 36, 79), his entire net income of $15,955.23 for personal services rendered for the period from October 2, 1937, until his remarriage on December 8, 1937 (R. 36, 80), and $2,963.89 representing one-half of his earnings for personal services for the period from his remarriage until the end of the taxable year (R. 36, 81). The sum of $28,941.85, being one-half of the petitioner's personal earnings for

the period from January 1, 1937, to October 2, 1937, when his wife obtained the final decree of divorce, was reported in the 1937 income tax return of Gertrude Martha Somerville (R. 36).

In determining the income-tax deficiencies here in controversy (R. 6–11) the Commissioner of Internal Revenue added to the gross income reported by the petitioner for the years 1936 and 1937 the one-half of the net earnings received by him during the period from September 1, 1936, to October 2, 1937, for personal services rendered which had been reported in the income-tax returns of Gertrude Martha Somerville for those years. The Commissioner explained that his action in so treating the personal earnings of the petitioner for this period was due to the fact that under the property-settlement agreement entered into by the petitioner and his wife the earnings of the petitioner for this period became his separate property and therefore taxable entirely to him (R. 8–9, 10). The Commissioner's determination was sustained by the Board of Tax Appeals (R. 12–23).

In the property-settlement agreement (R. 41–71) entered into by the petitioner and his wife on September 1, 1936, it was stated that whereas unhappy differences had arisen between the parties which made it impossible for them to live together, and that since they must henceforth live separate and apart (R. 41–42)—

> it is the desire and intent, finally and absolutely, of said parties, by this indenture, to settle and forever adjust, and have settled and forever adjusted between themselves, all of their

> mutual and respective present and future property rights, both as to the properties which either may claim to be community property, and also as to the separate estate of each, and it is their desire and intent to settle and adjust, finally and absolutely, by this indenture, any and all claim or claims for alimony, separate maintenance, counsel or attorney's fees, or costs of Court in any action that may be brought for a divorce, or any action that may now be pending, between said parties, or in any action at law or other litigation, or otherwise, which either of the parties hereto may or might hereafter make one against the other * * *

The agreement then provided at great length and in great detail for the disposition of a multitude of business and domestic problems, including the settlement of interests in money on hand and all property and assets owned by them individually or as community property. It also provided that, after the date of its execution, income-tax assessments "due, paid, or payable anywhere" upon the income of the wife "are to be borne and paid for solely by" the wife and not by the petitioner (R. 66). Any taxes which might become due upon the income of the parties prior to the execution of the agreement were to be borne by them equally (R. 67).

Among the material provisions of the property-settlement agreement were the following (the term "first party" being used to designate the wife and the term "second party" being used to designate the petitioner) (R. 42, 44, 49–50, 68–69):

> Whereas it is further desired and agreed on the part of the parties hereto, finally and abso-

It is further mutually understood and agreed that each of the parties may for themselves, independently of the other, control or do business in all matters the same as though he or she were single.

It is further understood and agreed that in making this final settlement of property rights that each of the parties hereto waives, relinquishes and forever surrenders all claim or claims of every kind or nature which she or he has or might hereafter acquire in or to or against the property of the other now held or hereafter acquired, including the rights of inheritance in case of death intestate or testate, which right each hereby expressly waives in favor of the heirs of the other.

It is further mutually understood and agreed that each of the parties hereto, their respective heirs, executors, administrators or assigns, shall, at any and all times, execute any paper that may be necessary to be executed for the purpose of giving full force and effect to these presents and to the covenants, provisions and agreements herein contained.

* * * * *

The agreement contained elaborate provisions for determining the amount of the petitioner's "net income" which was to be paid to the wife under the provisions set out above (R. 44–49). It also contained detailed provision for the use and distribution of the cash which petitioner had on hand on the date the agreement was executed (R. 53–57). These and other provisions of the agreement relating to the division of specific properties and the custody and support of their minor child are important in this proceeding

only because they demonstrate the completeness with which all their property and marital relations were settled.

SUMMARY OF ARGUMENT

The petitioner and his wife, due to marital difficulties, separated prior to September 1, 1936. On that date they entered into a property-settlement agreement which provided for division of all their property, settlement of all claims against each other, and custody and maintenance of their minor child. A final decree of divorce was granted to the petitioner's wife on October 2, 1937.

Under California law the personal earnings of a husband and wife become community property, and for the period here involved such income is taxable one-half to each spouse for federal income tax purposes. However, the laws of California recognize the right of husband and wife, by contract, to alter their respective property rights, changing separate property into community property or community property into separate property.

This Court has consistently held that where married persons, domiciled in a community property state, make an agreement, valid under state law, whereby the future earnings of either is converted into his or her separate property such agreements will be given effect in the administration of the federal income tax laws.

Under the agreement between this petitioner and his wife, when the agreement is considered as a whole, it is clear that the parties intended all future earnings of the petitioner to be his separate property. His

undertaking to pay his wife one-half of his "net income," as computed in accordance with the agreement, for the next two years after execution of the agreement does not require a construction of the agreement to the effect that the petitioner's earnings remained community property until the final decree of divorce was granted. In fact, such a construction would be contrary to the intention of the parties and the provisions of the agreement.

ARGUMENT

The Board of Tax Appeals did not err in holding that the petitioner's personal earnings subsequent to execution of the property settlement with his wife are taxable entirely to him

In this case the petitioner and Gertrude Martha Somerville had been married some years prior to September 1, 1936, and had resided together in California until sometime prior to that date (R. 15). On that date they entered into a property settlement agreement (R. 41–71), the material portions of which are set out in the foregoing statement. On September 28, 1936, Gertrude Martha Somerville obtained an interlocutory decree of divorce from the petitioner which was made final on October 2, 1937 (R. 15, 34, 37–40).

The only question involved in this proceeding is whether the petitioner's earnings for the period from September 1, 1936, to and including October 1, 1937, for personal services rendered by him was community property taxable one-half to him and one-half to his wife, or whether, by reason of the property-settlement

agreement, such personal earnings constituted separate property of the petitioner taxable entirely to him.

It is not denied that in the absence of any agreement of the spouses to the contrary the personal earnings of the petitioner for the period involved would have constituted community property under the laws of California and taxable one-half to each for federal income-tax purposes. *United States* v. *Malcolm,* 282 U. S. 792; Civil Code of California, Section 161a, *supra.* The Commissioner of Internal Revenue ruled, however, that the property-settlement agreement of September 1, 1936, had the effect of converting the petitioner's personal earnings subsequent to that date into his separate property (R. 6–11). His determination was sustained by the Board of Tax Appeals (R. 13–23). We submit the decision of the Board is right and should be affirmed.

The Civil Code of California (Sections 158 and 159) recognizes the right of married persons residing in California to make contracts with respect to their property. Under such contracts community property may be converted into the separate property of either spouse or the separate property of either may be converted into community property. See *Helvering* v. *Hickman,* 70 F. (2d) 985 (C. C. A. 9th), and cases cited. As this Court said in *Black* v. *Commissioner,* 114 F. (2d) 355, 358:

> A consideration of the many cases bearing on this subject would serve merely to lengthen the opinion. This court has consistently upheld the proposition that where married persons, domiciled in a community property state, make

> an agreement, valid under the local law, whereby the future earnings of each shall not become community property, but shall remain the separate property of the recipient, such agreement will be recognized in applying the federal income tax law. *Helvering* v. *Hickman,* 9 Cir., 70 F. 2d 985; *Van Every* v. *Commissioner,* 9 Cir. 108 F. 2d 650; *Sparkman* v. *Commissioner,* 9 Cir., 112 F. 2d 774.

See, also, *Woodall* v. *Commissioner,* 105 F. (2d) 474 (C. C. A. 9th), certiorari denied, 309 U. S. 655; *Boland* v. *Commissioner,* 118 F. (2d) 622 (C. C. A. 9th); *Marshall* v. *United States,* 26 F. Supp. 474 (C. Cls.), certiorari denied, 308 U. S. 597.

We do not understand the petitioner to question the above principles enunciated by this Court and the courts of California. His argument (Br. 6–27) is based upon the proposition that in the absence of an agreement to the contrary the earnings of the husband and wife are community property under the laws of California (Br. 6), which is not denied by the Commissioner; that the question for determination is whether under the property-settlement agreement the subsequent earnings of the petitioner became his separate property (Br. 7), with which the Commissioner agrees; and that the property-settlement agreement entered into with his wife did not convert his personal earnings into his separate property (Br. 9). With the latter contention the Commissioner does not agree.

The petitioner's argument that the property-settlement agreement did not convert his personal earnings thereafter into his separate property appears to be

based upon the proposition that "there is no provision in the agreement to the effect that the subsequent earnings of each spouse are to be the sole and separate property of the earner" (Br. 13).

Some of the cases particularly relied upon by the petitioner in support of this argument are cases decided by the California courts in which the widow, after the death of her husband, sought a family allowance during the period of the administration of his estate (Br. 20–26). In each of those cases the spouses had entered into a property-settlement agreement prior to the death of the husband, and the allowance was contested by the estate on the ground that the wife had waived it under the terms of the property-settlement agreement. But those cases are different from the instant case in important respects. In the first place, those cases, like the instant case, depended upon the interpretation of the property settlement involved. But of far greater importance is the fact that the question involved was whether the widow had waived her family allowance, and that depended upon a construction of the property-settlement agreement. No such question is involved here.

In this connection, however, it is to be noted that if the same question were at issue in the instant case a court might well reach a contrary conclusion because, in addition to the initial inducement clause stating the reason for the agreement and the intention of the parties executing it (R. 41–42), it is expressly provided that the arrangement for the payment of one-half of petitioner's net income to his wife for two

years should be in full and final settlement of any and all claims of either against the other, other than as otherwise disposed of in the agreement, "whether in law or in equity or in *probate*"; also in full settlement of "any and all claim or claims of community property which either might or could make against the other"; and, finally, in full and final settlement of any and all future claims which either might assert against the other, "of whatsoever kind or nature, whether in law and/or in equity and/or in *probate*" (R. 49–50). [Italics supplied.] Furthermore, by Article XIV of the agreement (R. 67), the petitioner's wife expressly waived and released any claim for attorney's fees or costs in connection with any claim or claims, "either in law, equity or probate," whether valid or invalid, against the petitioner, and whether arising or made prior or subsequent to the agreement or arising out of the signing of the agreement.

We submit that, were the question whether the petitioner's wife had waived her right to a family allowance involved here, which it is not, it could justifiably be concluded, from the terms of the agreement as a whole, including the above provisions, that the wife had waived any right to a family allowance. Compare *In re Davis,* 106 Cal. 453.

The decisions in *Biggi* v. *Biggi,* 98 Cal. 35, and *Estate of Hurley,* 28 Cal. App. (2d) 584, cited by petitioner (Br. 15, 17), are equally inapplicable here. The former decision dealt with disposition of a parcel of real estate covered by a general property settlement, while the latter dealt with the surviving husband's rights in the estate of his deceased wife under

a property-settlement agreement, which was in no way comparable with the agreement executed by this petitioner and his wife.

While the decisions of this Court cited above are determinative of the questions of law here involved, it still remains to be determined whether the property-settlement agreement involved in this case had the effect of converting the petitioner's personal earnings into his separate property. We submit that when the agreement is considered as a whole, as it must be, in the light of the expressed intentions of the parties and the purpose which they accomplished, there can be no basis for concluding that the petitioner's personal earnings remained community property after execution of the agreement.

The property settlement itself (R. 41–71) is too long and wordy to justify a full analysis here. But the purpose of entering into the agreement (R. 41–42), and the results accomplished are clear. The parties had come to the end of their marital career and already were living apart without any prospect of reconciliation. They intended, and by the agreement accomplished, a complete division of all property owned by them, a settlement of all rights and claims which either might assert, and assured the continued support and custody of their minor child.

While the agreement must be construed as a whole to arrive at a correct solution of this appeal, the income involved is one-half of the amount which the petitioner treated in his income tax returns as community income for the period from September 1, 1936, through October 1, 1937, although not necessarily that

part of the petitioner's "net income," computed in accordance with the agreement (R. 44–49), which was payable to the petitioner's wife for the period prior to entry of the final divorce decree. The petitioner contends that such income from personal services was community property under the laws of California until entry of the final divorce decree on October 2, 1937, but makes no such contention with respect to such income, a part of which had to be paid to his wife during the balance of the two-year period following the execution of the property-settlement agreement.

In this respect the instant case does not differ materially from *Boland* v. *Commissioner,* 118 F. (2d) 622 (C. C. A. 9th), and *Woodall* v. *Commissioner,* 105 F. (2d) 474 (C. C. A. 9th). In each case the spouses entered into a property-settlement agreement similar to the one here involved. In the *Boland* case the agreement provided for payment of a percentage of the taxpayer's personal earnings to his wife for life or until she remarry, whether divorced or not, while in the *Woodall* case the taxpayer's husband received substantially one-half her earnings under their understanding of the agreement until they were finally divorced. On authority of those two decisions, and other decisions of this Court cited above, it must be concluded that this petitioner's personal earnings subsequent to execution of the property-settlement agreement with his wife were his separate property and taxable entirely to him.

CONCLUSION

The decision of the Board of Tax Appeals is right. It is fully supported by the facts and the law and should be affirmed.

Respectfully submitted.

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IN THE

United States Circuit Court of Appeals

FOR THE NINTH CIRCUIT

GEORGE J. SOMERVILLE, also known as SLIM SUMMERVILLE,

Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,

Respondent.

PETITIONER'S REPLY BRIEF.

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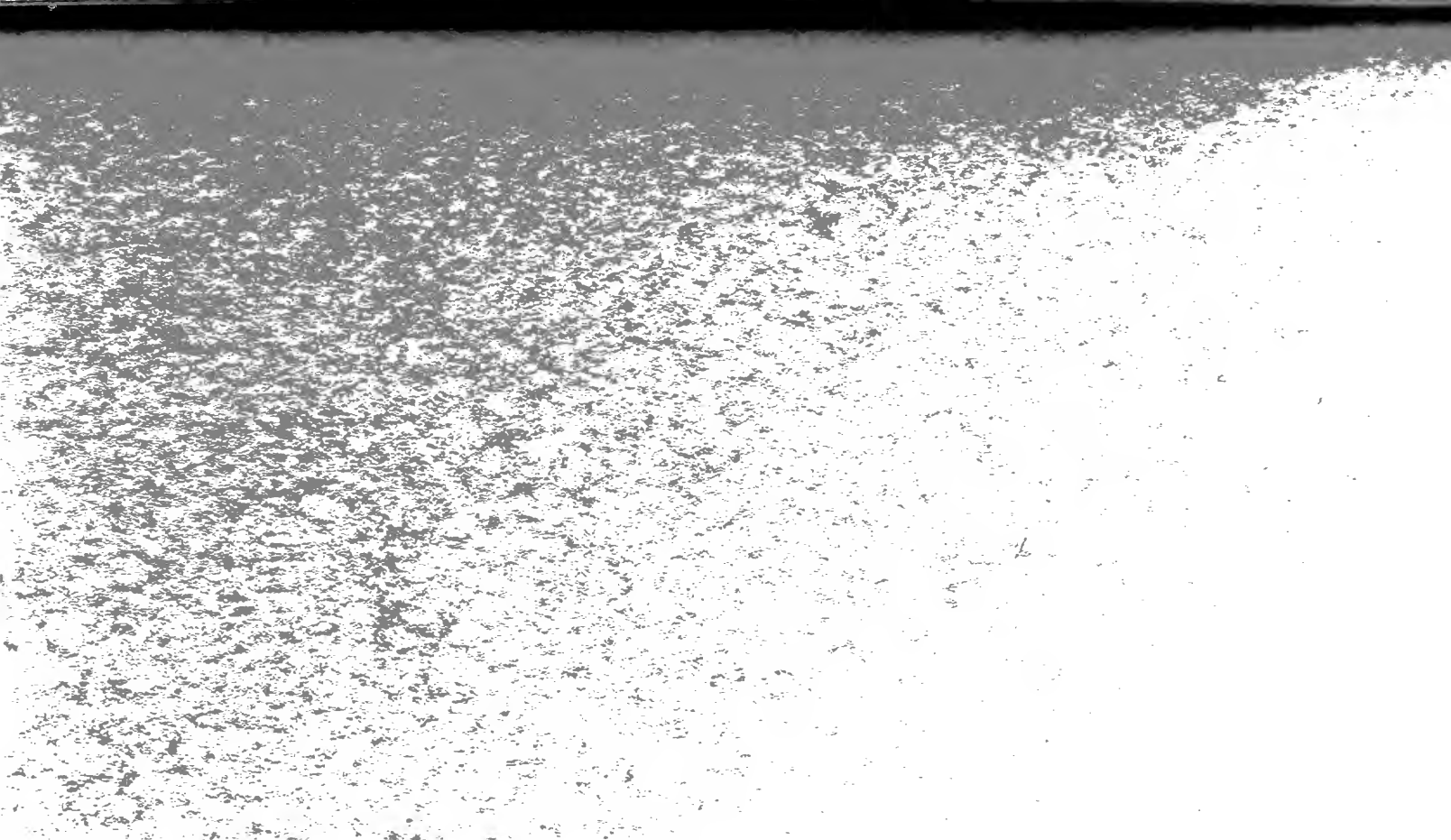

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No. 9857.

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COMMISSIONER OF INTERNAL REVENUE,

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PETITIONER'S REPLY BRIEF.

Preliminary Statement.

The jurisdictional statement, statement of facts and specifications of error are contained in petitioner's opening brief (pages 1-4). This brief is devoted solely to answering the argument contained in respondent's brief.

ARGUMENT.

Petitioner and respondent agree that the question involved in this case is whether the contract entered into by petitioner and his wife destroyed the community character of petitioner's earnings during the continuance of the marriage relationship. (Resp. Br. p. 14.)

The authorities cited by petitioner in his opening brief, with two exceptions hereinafter specifically referred to, are disposed of by respondent in the following language:

> "Some of the cases particularly relied upon by the petitioner in support of this argument are cases decided by the California courts in which the widow, after the death of her husband, sought a family allowance during the period of the administration of his estate. (Br. 20-26.) In each of those cases the spouses had entered into a property-settlement agreement prior to the death of the husband, and the allowance was contested by the estate on the ground that the wife had waived it under the terms of the property-settlement agreement. But those cases are different from the instant case in important respects. In the first place, those cases, like the instant case, depended upon the interpretation of the property settlement involved. But of far greater importance is the fact that the question involved was whether the widow had waived her family allowance, and that depended upon a construction of the property-settlement agreement. No such question is involved here." (Resp. Br. p. 15.)

In the first place the cases cited by petitioner all dealt with the construction of property settlement agreements and more particularly whether one of the parties had waived a property right that grew from the marriage relation. The right to a probate homestead, family allowance or to share in the estate of a deceased spouse through a successful contest are all valuable property rights and all of said rights are incident to and founded upon the marriage relationship. Likewise the right of a spouse to one-half of the community income is dependent upon that relationship. Decisions involving the construction of property

settlement agreements should be considered in point whether they deal with future earnings or some other property rights of the parties. It must be remembered that all of these elements of property settlement agreements, namely, probate homestead, family allowance and future community earnings, are authorized by and founded upon Sections 158 and 159 of the Civil Code of the State of California. Those sections do not refer solely to the question of future income but authorize a husband and wife to contract generally with relation to their property. Therefore, it is not sound to contend that decisions are not in point which interpret property settlement agreements because the question involved is whether or not the spouse has waived a probate homestead or family allowance.

We concede that no one but a husband and wife can own community property and when their status as such is dissolved, they cannot thereafter acquire community property. Therefore, there is no question but what petitioner's income after the final divorce constitutes his separate income and is taxable with reference to that status.

Respondent makes no mention of *Sherman v. Commissioner* (9 Cir.), 76 Fed. (2d) 810, cited in petitioner's brief (p. 10). That case deals with the construction of a property settlement agreement between a husband and wife residing in California. It was contended by the wife that the agreement had the effect of making the future earnings of her husband his sole and separate property, and she and her husband testified before the Board that it was their intention to so provide in the agreement. In that case, as in the case before the Court, the parties had made various provisions with relation to their property, but had made no provision changing the character of the

future earnings of the husband. This Court, in the following clear and explicit language, held that the earnings of the husband, therefore, were community:

> "Bearing in mind that the wife has an immediate vested interest in one-half of the earnings of the husband, in the absence of any conveyance or agreement by her transferring her right to the husband, it would be retained by her and be subject to tax as her income."
>
> *Sherman v. Commissioner,* 76 Fed. (2d) 810-811.

The only authorities cited by petitioner in his opening brief that are specifically referred to by respondent are *Biggi v. Biggi,* 98 Cal. 39, and *Estate of Hurley,* 28 Cal. App. (2d) 584. In referring to those cases the respondent makes the following comment:

> "The decisions in *Biggi v. Biggi,* 98 Cal. 35, and *Estate of Hurley,* 28 Cal. App. (2d) 584, cited by petitioner (Br. 15, 17), are equally inapplicable here. The former decision dealt with disposition of a parcel of real estate covered by a general property settlement, while the latter dealt with the surviving husband's rights in the estate of his deceased wife under a property-settlement agreement, which was in no way comparable with the agreement executed by this petitioner and his wife." (Resp. Br. pp. 16 and 17.)

We will not again set forth in detail the facts and holdings of the Court in those cases, but refer the Court to our opening brief, pages 15-17, for *Biggi v. Biggi* and pages 17-20 for *Estate of Hurley.* Suffice it to say that each of said cases dealt with the construction of a property settlement agreement between a husband and wife

and the law of California relative to the interpretation of the language of such agreements, especially wherein the waiver of a property right is involved.

On three different instances the respondent reverts to the statement "When the agreement is considered as a whole, it is clear that the parties intended all future earnings of the petitioner to be his separate property." (Resp. Br. pp. 11 and 17.) We agree to the proposition that a contract must be considered as a whole, especially when there is no specific provision that effectually disposes of a problem that arises under it. However, as pointed out in our opening brief, the specific provisions of a contract control over the general provisions. (Pet. Br. p. 14.) Under the agreement that the Court is here called upon to construe, it was specifically provided that the wife is to receive and retain one-half of petitioner's earnings for the period in question. [R. p. 44.] Having retained and not transferred her community one-half interest in those earnings, she comes within the holding of *Sherman v. Commissioner, supra,* hereinabove cited and quoted from.

Respondent closes his brief by asserting:

> "In this respect the instant case does not differ materially from *Boland v. Commissioner,* 118 F. (2d) 622 (C. C. A. 9th), and *Woodall v. Commissioner,* 105 F. (2d) 474 (C. C. A. 9th). In each case the spouses entered into a property-settlement agreement similar to the one here involved. In the *Boland* case the agreement provided for payment of a percentage of the taxpayer's personal earnings to his wife for life or until she remarry, whether divorced or not, while in the *Woodall* case the taxpayer's husband received substantially one-half her earnings under their understanding of the agreement until they were

finally divorced. On authority of those two decisions, and other decisions of this Court cited above, it must be concluded that this petitioner's personal earnings subsequent to execution of the property-settlement agreement with his wife were his separate property and taxable entirely to him." (Resp. Br. p. 18.)

This statement betrays the weakness of respondent's position for the two cases cited are not authority for anything that this Court has to decide. In *Boland v. Commissioner,* 118 Fed. (2d) 622 (9th Circuit), the agreement provided:

> "The parties hereto also being desirous of settling their respective rights in and to the community property of the parties hereto now existing and of . . . fixing and determining the character of the property hereafter to be acquired by the parties hereto, and . . . and said party of the second part hereby agrees that the portion of the income of the party of the first part not hereinabove in paragraph (1) hereof assigned to the party of the second part and any proceeds from the investment or reinvestment of said portion of said income shall be and become the separate property of the party of the first part."

In construing that language, this Court rightfully held:

> "This evidences a fixed determination to strip any future income of its community character, but the operative parts of the agreement are also inconsistent with the concept of community property."

In *Woodall v. Commissioner,* 105 Fed. (2d) 474-475, 476, the Court construed a property settlement between a husband and wife, which, according to the opinion of the Court, contained the following provision with respect to the future earnings of the parties:

> "All property hereafter acquired, in whatsoever manner, and all earnings which may be acquired by either of the parties, shall be the sole and separate property of the party so acquiring it, free from all claims, rights or interests of the other."

If the agreement between the Somervilles contained such language, the petitioner would not now be before this Court.

The further and main contention in the *Woodall* case is stated in this language, at page 477 of the opinion:

> "The petitioner contends that Section 169 of the Civil Code of California is not applicable; that the written property settlement agreement of April 20, 1932, was modified, abrogated, or superseded by an oral agreement made immediately upon the signing of the written agreement; that the earnings of both spouses are community property until the entry of the final decree of divorce; that the Board failed to distinguish between the circumstances which existed prior and subsequent to April 20, 1932 (the date of the entry of the interlocutory decree of divorce);"

and is disposed of by the Court in the following manner, at page 478 of the opinion:

> "So far as the testimony of petitioner and Gallery to the effect that the written agreement was nullified, almost before the signatures were dry, by an oral agreement, we are of opinion that the Board did not err in declining to find that such agreement was in fact made. The Board saw and heard the witnesses and weighed the testimony; neither process is a function of this court."

When respondent rests his case on authorities such as the two just mentioned, we believe that we have every right to assert that he has a weak foundation in law for the position which he is attempting to maintain.

Conclusion.

The decision of the Board of Tax Appeals is contrary to the facts and the law and should be reversed.

Respectfully submitted,

EDWARD L. CONROY,
DON CONROY,
Attorneys for Petitioner.

APPENDIX.

Statutes Involved.

Civil Code of State of California, Div. 1, Pt. 3, Tit. 1, Ch. 3.

"#157. In other respects their interests separate. Neither husband nor wife has any interest in the property of the other, but neither can be excluded from the other's dwelling. (Enacted 1872.)"

"#158. Husband and wife may make contracts. Either husband or wife may enter into any engagement or transaction with the other, or with any other person, respecting property, which either might if unmarried; subject, in transactions between themselves, to the general rules which control the actions of persons occupying the confidential relations with each other, as defined by the title on trusts. (Enacted 1872.)"

"161a. (Interests in community property.) The respective interests of the husband and wife in community property during continuance of the marriage relation are present, existing and equal interests under the management and control of the husband as is provided in sections 172 and 172a of the Civil Code. This section shall be construed as defining the respective interests and rights of husband and wife in the community property. (Added by Stats. 1927, p. 484.)"